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REPORT OF THE LIABILITY AND PROPERTY INSURANCE MARKETS STUDY COMMISSION



**REPORT TO THE
1987 GENERAL ASSEMBLY
OF NORTH CAROLINA**

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INTRODUCTION

Many study reports begin with summaries of the recommendations of the study group, and then proceed to describe the information that the group discovered and that led the group to its factual conclusions and recommendations.

Sometimes this practice is helpful to the reader because it alerts the reader to the direction of the report. When the subject matter of the report is complex as that in this report, this practice does not serve the reader well; because the purpose of a report is to provide the reader with as much background as possible in order that the reader may be able to make an informed judgment about the recommendations. Such a sneak preview of the ultimate conclusions of the study group may tempt even the most conscientious reader to rely on the summary rather than reading the entire report and developing the necessary background to judge the conclusions of the study committee.

The significance of the subject matter of this report cannot be overstated. Liability, casualty, and property insurance touches everyone either directly as a homeowner, professional, or businessman or indirectly as a consumer or as a citizen of a municipality or county that attempts to provide insurance protection against foreseeable and unforeseeable losses.

The General Assembly last studied the problems surrounding the liability and property insurance market in 1975 during the "crisis in medical malpractice insurance." Some actions were

taken by the General Assembly to address the issue, but basically, due to the cyclical nature of that and all insurance marketing problems, the crisis abated with the creation of a physician funded mutual insurance program and the reentry into the medical malpractice insurance market of a major underwriter. On file in the Legislative Library is a Report of the North Carolina Professional Liability Insurance Study Commission dated March 12, 1976 which discusses the study and its conclusions.

It is interesting to note that the apparent cyclical nature of problems faced in liability insurance marketing have expanded this time not only to include medical malpractice insurance (which the General Assembly again chose to study, separately) but all forms of liability and property insurance (which serve as the focus of this study).

BACKGROUND

The subject of this study, the situation surrounding the marketing of liability and property insurance, is an extremely complex one. The subject of liability insurance was addressed in parts of 21 bills that were considered and ratified by the 1985 General Assembly (See Appendix A for a list of those bills). Among those was House Bill 763, the original bill that authorized this study which was introduced by Representative Hasty.

Appendix B --"Basic Concepts" contains a discussion of concepts and terms that should be understood by a person who wants to understand the problems considered by this Commission.

During the public hearings and other deliberations by the Commission it became apparent to the Commissioners that whether or not there was a "crisis," the marketing of liability and property insurance affected virtually everyone in this State in one way or another.

At the hearings, the Commission heard from individual citizens, small businesses, large businesses, insurance agents, insurance companies, attorneys, other professionals, daycare establishments, local governments, and many others.

The five public hearings were replete with "horror stories" about:

***Insurance companies "losing billions of dollars".

***Foreign reinsurers withdrawing from the American market because it was not profitable forcing American insurers to reduce their capacity and ability to write insurance.

***Insurance agents losing contracts with companies for whom they had written policies for many years, without notice or reasons.

***Mid-term cancellations and short notices of intent not to renew insurance policies prohibiting or limiting the opportunity to obtain replacement coverage.

***Cities and counties, as well as private businesses and professionals, having their insurance cancelled or their premiums being increased anywhere from 50% to 1700% or more, despite having not made claims under their insurance policies, forcing them to decide whether to go out of business or, in the cases of local governments, whether or not to "go bare."

***People with homes, or people wanting to buy homes and needing insurance as a precondition to obtaining financing, being unable to obtain fire and property insurance because of withdrawal of insurance companies from certain areas of the State.

And many other effects of the liability and property insurance market situation.

The Commission did not attempt to assess "blame" for the market situation noting that all involved parties could share the responsibility for the perceived "crisis."

The Commission sought to determine what effects the liability and property market situation was having on the citizens of the State and to determine what legislative actions could be taken to assure the citizens of the State of the availability of an ample supply of insurance, at reasonable cost, and with reasonable coverages.

CONFLICTING INFORMATION

In order to provide an example of the conflicting information that was provided to the Commission; conflicts which made the work of the Commission difficult and at times confusing, the following background statements are provided.

NIMLO REPORT ON THE MUNICIPAL LIABILITY INSURANCE MARKET¹

The liability insurance industry, including the worldwide reinsurance market which underwrites a major portion of the liability coverage provided to both public and private insureds, is experiencing unprecedented losses, characterized by some experts as the worst financial crisis in the property/casualty industry in history. Insurance experts suggest a myriad of causes, many of which contributed directly to the present crisis and many of which are better explained as insurance industry excuses. The purpose of this report is to provide a better understanding of how the problem developed, the factors which contributed, the insurance industry's response and, most importantly, where entities seeking insurance should look for a solution.

¹This explanation of the present "crisis" in the municipal liability insurance market is taken in large part from a Report of the Municipal and Public Official Liability Insurance Committee of the National Institute of Municipal Law Officers (1985-86).

A few statistics will put the problem in perspective:

- *** The insurance industry has lost more than \$34 billion in the past two years; more than the total lost in the previous twenty-five years.
- *** According to A. M. Best Company, in 1984 the liability insurance industry lost \$3.8 billion compared with earnings of \$2.5 billion in 1983. (This is the first annual loss for the liability insurance industry since 1906.)
- *** As of April 3, 1985, the casualty facultative reinsurance capacity in the United States decreased \$100.5 million.
- *** The industry experienced underwriting losses of \$785.5 million in 1982, compared with \$468.9 million in 1981, while the combined loss and expense ratio reached 105.5% of earned premium.

Among some of the more significant factors that contributed, at least in part, to the present liability insurance crisis are the following:

- **** A continuation of the traditional relationship between primary and excess reinsurers.
- **** A significant increase in the number of competitors in the reinsurance market and a corresponding decrease in its sophistication.

**** Increased competition in the primary insurance market due to a corresponding increase in inflation and a resulting development of cash flow underwriting.

**** A developing deficiency in the compilation of sound actuarial data accompanied by a corresponding increase in volume and complexity of claims and litigation.

**** Unsound underwriting practices.

**** Increases in litigation and attendant expenses.

In the past few years, because of high interest rates, insurance companies have invested their premiums and recovered handsome profits, thereby subsidizing the ever-increasing claim losses that were being experienced. While interest rates hovered near 20% a few years ago, the insurance industry began to engage in what is known as "cash flow underwriting" -- the practice of selling insurance coverages at cut-rate prices with the intent of making up on reinvestments. This phenomenon brought unknowledgeable participants into both the primary insurance market (the portion of the industry that actually writes insurance policies), and into the reinsurance market (the portion of the industry that underwrites primary carriers through reinsurance treaties). When a company writes a large liability policy, particularly to an insured perceived as high-risk, the carrier turns to larger companies for reinsurance underwriting assistance.

When the recent fall in interest rates occurred, companies were left without the anticipated investment income to subsidize claim losses. They were then in a position of having inadequate premiums and high-risk policies. At the same time, the reinsurance market (led by influential companies such as Lloyd's of London) curtailed their reinsurance treaties. The net result: The insurance industry simply lost the capacity to underwrite high-risk policies. Once the reinsurance capacity was lost and interest rates had fallen, the industry had placed itself in the untenable position of holding anticipated incurred losses which far exceeded foreseeable income.

The insurance industry has taken numerous steps to reduce its losses. The major changes that are taking or have taken place are:

- (A) Cancellation of major exposure clients
- (B) Restriction of new business
- (C) Reduction of coverages
- (D) Increase in premiums
- (E) Curtailment of underwriting of High-Risk Business
- (F) Selective underwriting criteria

Each of these responses is analyzed separately below.

A. CANCELLATION OF MAJOR EXPOSURE CLIENTS. A number of insurers have stopped underwriting municipal and other liability coverage completely. Others have temporarily discontinued writing liability insurance. Municipalities are not the only entities

that the industry has targeted for cancellation. Others include the airline industry, professionals (including doctors and accountants), and industries which are likely targets of products liability lawsuits. Day-care centers have become a high risk business because of sexual abuse cases. Liquor stores have been denied liability coverages because they now may be liable for death and injury caused by drunken customers.

Because of the rapid and continuing rise in cancellations, the National Association of Insurance Commissioners received outcries of "unfair and deceptive trade practices" by insurers. The Commission established new guidelines relating to midterm cancellations of coverage, providing that insurers wishing to cancel should do so only at the expiration of the policy itself, or alternatively, should provide for other reinsurance. The new guideline also provide that at least thirty days advance notice be given for non-renewals of policies in order to allow the insured to seek alternative coverages.²

B. RESTRICTION OF NEW BUSINESS. Another response by the industry has been to simply refuse to underwrite new business. This, coupled with the withdrawal of the major municipal liability carriers from the market, has posed further unforeseen and uncontrollable difficulties for municipalities seeking liability coverage. At the same time that primary carriers are withdrawing

²These guidelines were contained in the legislation passed by the North Carolina General Assembly during the one day special session during February, 1986.

rapidly from this and other markets, the reinsurers who have rapidly proliferated the market in recent years are "renegotiating" their treaties with the few primary carriers still in the business of providing municipal liability coverage. As a result, the companies which are willing to write municipal liability coverage often are unable to do so because of inadequate reserves and unavailable reinsurance capacity.

C. REDUCTION OF COVERAGES. Another by-product of the present insurance crisis is that the Insurance Services Office (ISO), the entity which provides form policies for the commercial insurance industry, has developed a new comprehensive general liability (C.G.L.) policy which significantly diminishes protection to the insured in a number of respects. For example, the revised form deletes pollution coverage, which historically was included but with the "sudden and accidental" limitation. However, due to recent developments in case law, the industry has chosen to completely withdraw from writing pollution coverage of any sort.

The new ISO form further modifies existing comprehensive general liability forms by including defense costs within aggregate limits. Due to the ever increasing defense costs of litigation, including defense costs within the aggregate limits will significantly diminish indemnification afforded under primary coverages. In 1984, one quarter of earned insurance premiums in general liability coverages (approximately \$1.5 billion) were

spent on attorney's fees, a 500% increase over the past thirty years. As a consequence, umbrella coverages will likely become even more expensive. ISO is also considering an optional endorsement to provide for the sharing of legal costs by the insured.

The new ISO form will also change "occurrence" coverage to "claims made" coverage because of the industry's experience with litigation arising out of coverages for asbestos, DES, radiation, agent orange, and other "long tail" risks. Much of the burden is being passed to those perceived as high risk insureds, such as municipalities. If coverages change from occurrence to claims-made format, incidents that were previously insured (because they occurred during the policy period), will often times be uninsured unless a claim has actually been made against the insured during the coverage period.

The new ISO C.G.L. form will also contain an extended reporting period restriction whereby claims made more than sixty days after the policy expiration will not be covered unless the insured purchases an "unlimited extended reporting period," for which the premium will approximate 200% of the premium for the prior policy year. Thus, unless the buyer renews his coverage with carrier X, he will be compelled to purchase the extended reporting period coverage at up to 200% additional cost. If, on the other hand, carrier X chooses to cancel or non-renew of if the

buyer seeks coverage from carrier Y, a 200% premium will be required to keep the extended coverage.

D. INCREASE IN PREMIUMS. Another response by the industry has been to pass on the cost of the industry's underwriting losses through increased premiums to those perceived as high-risk insureds. No direct link need exist between actual losses and high premiums: a mere perception by the industry that the particular insured falls into a high-risk category provides the industry with a sufficient basis for escalating premiums, regardless of actual experience.

At the same time as they increase premiums, insurers are also demanding higher deductibles, higher self-insured retentions and stricter reporting requirements.

E. CURTAIL UNDERWRITING OF HIGH-RISK COVERAGES. Since the beginning of 1985, a number of insurers have totally curtailed underwriting liability coverages for public entities and others continue to withdraw from the market. As of August, 1985, twelve major carriers have stopped writing coverage: all within the last two years. The stated reasons for the growing reluctance to insure political entities: fear of growing losses resulting from the erosion of governmental immunity by the courts. Insurers also express an aversion to competitive bidding, arguing that they are unable to win renewals if another insurer underprices them. Third, reinsurers are refusing public entity risks, thereby forcing the primary insurers to underwrite more of the exposure

themselves if they have the financial capacity, or to refuse to write the coverage if they do not.

F. SELECTIVE UNDERWRITING CRITERIA. Another industry response has been to develop underwriting criteria by: limiting the scope, amount, and duration of coverages; establishing overlapping population and budgetary restrictions on the entities that they will insure; demanding higher deductibles and self-insured retentions; adding new "standard" exclusions; and rewriting coverages to conform with the new ISO "claims made" C.G.L. forms.

LONG-TERM SOLUTIONS:

In light of the revolution occurring in the municipal liability insurance market, cities must immediately look to other options, such as self-insurance, pooling, or purchase of commercial coverage with higher deductibles. If the third option (purchase of commercial coverage with higher deductibles) is chosen, the insured must establish sound budgetary restrictions to provide revenue necessary to counteract the reduction of coverages because of the new ISO exclusions.

It is suggested that larger cities may be able to survive the crisis in the insurance industry by solely self-insuring (which is in effect "uninsuring"), but small municipalities can ill afford the inherent risks of doing so. A large judgment can place a small city in such financial straits that it is forced to either increase taxes, issue bonds, or file a petition for bankruptcy.

For small cities, self-insurance pooling is becoming an increasingly attractive alternative. The cost of coverages is often significantly less than is coverage on the traditional insurance market and the coverage itself is much broader and much better adapted in most instances to the risks which a small municipality is attempting to insure. A caveat is in order--self-insurance pools can easily find themselves in the same position as the insurance industry finds itself. Most self-insurance pools buy reinsurance through the same market that has recently retrenched. Self-insurance pools often engage in the same investment and marketing practices that led to the problems in the insurance industry. Self-insurance pools are becoming increasingly aware of the need to restrict their coverages in the same manner as the insurance industry has done through the ISO form revisions. Another alternative is the purchase of commercial insurance coverage with significantly higher deductibles than in the past.

By proposing a higher deductible, a municipality sends a message to potential underwriters that it is both aware of the increasing exposures and willing to underwrite a larger portion itself. A comprehensive risk management program which identifies significant risks, establishes methods for their reduction, and explores alternatives by which those that are likely to occur are financed will make a municipality a much more attractive insured.

Regardless of the alternative chosen, long-range risk management and litigation cost control practices must become standard procedure. With the continued proliferation of litigation of all sorts, municipalities will continue to be target defendants, and thus perceived as "high-risk" insureds. Therefore, it is safe to assume that even after the insurance industry has stabilized it will continue to respond to municipalities in the same manner as it has to the present crisis.

NORTH CAROLINA BAR ASSOCIATION POSITION¹

In recent months substantial attention has been focused on problems related to the cost and availability of liability insurance. Substantial disagreement has surfaced about both the severity and causes of these problems and a variety of special interest groups have become active participants in a continuing debate about them.

A number of major changes in the tort system have been proposed and are being actively pushed in state legislatures as one response to the liability insurance problem. Some groups describe the situation as a crisis in the tort system. The reporting date of two legislative study commissions has been accelerated to permit them to report to the 1986 Special Session of the legislature.

Legislation to effect fundamental changes in North Carolina's tort system should not be enacted in an emergency atmosphere that precludes full study of the problem and its causes and full consideration of courses of action that may offer viable solutions to it. Further, major changes in the legal system should not be undertaken without significant participation of lawyers any more than major change in medical practice should be legislated without involvement of physicians. The North Carolina Bar Association has

¹This is a condensation of the position paper entitled "REPORT OF THE SPECIAL COMMITTEE ON THE TORT LIABILITY SYSTEM" from the North Carolina Bar Association which was prepared by Robert G. Byrd, Professor of Law, UNC, and dated Friday, May 9, 1986.

traditionally assumed a major role in implementing law reform in this state. It is again prepared to do so. The President of the North Carolina Bar Association has appointed a committee of lawyers and law teachers to conduct a thorough study of the tort system, and criticisms of it, and the proposals for change. Committee members include attorneys representing claimants, defendants and insurers so that its deliberations will reflect both extensive knowledge and experience as well as a balanced perspective.

Before fundamental changes are made in North Carolina's tort law, careful study of four basic areas is needed:

- 1) to gain a better understanding of the causes and extent of the difficulties related to the costs and availability of liability insurance.
- 2) to determine whether or not the changes in tort law now under consideration are likely to affect the costs and availability of liability insurance in North Carolina.
- 3) to determine whether North Carolina loss experience provides the basis for the costs and availability problems encountered in North Carolina.
- 4) to evaluate the fairness of the present tort system as well as the fairness of the proposals for change in it.

Careful study is needed to gain a better understanding of the causes and extent of the difficulties related to the costs and availability of liability insurance.

Perceptions of the causes of the difficulties that have been experienced in obtaining liability insurance vary greatly. Among the factors frequently cited as causes are:

- increases in the number of tort claims,
- increases in the number of tort suits,
- increase in the size of jury verdicts and settlements,
- expanding concepts of tort liability,
- diminished requirements of proof to establish tort liability,
- high litigation costs,
- the economic cycle of the insurance industry,
- the substantial downturn in interest rates and its impacts on the earnings of insurance companies,
- poor business practices of insurance companies,
- inadequate regulation of the insurance industry,
- increasing complexity of business and professional practice,
- malpractice itself, and
- failure of the professions adequately to regulate and discipline their members.

Each of these factors may or may not have some basis in fact. Much of the focus on these factors to date, however, has been through the presentations of special interest groups which have tended to emphasize selective development of the factors that best

promote their positions. The need for an impartial and balanced study is critical.

Conflicting views exist concerning the extent of the difficulties that are present. For example, although physicians and medical malpractice insurers are in the forefront of demanding legislative action, other groups claim that malpractice liability insurance premiums paid by physicians are not unreasonable. Similarly, some groups assert that general tort reform is needed because the difficulties related to liability insurance are pervasive; however, others claim that the experience of insurance companies writing casualty insurance in North Carolina has been very favorable. Again, the need for careful study is clearly indicated.

Careful study is needed to determine whether or not the changes in tort law now under consideration are likely to affect the costs and availability of liability insurance in North Carolina.

Many of the proposed changes in tort law currently under consideration were adopted by some state legislatures in the mid 1970's. Some related changes were adopted in North Carolina. A number of studies have been made of the impact of these earlier changes in tort upon the costs and availability of liability insurance. Careful examination of these studies and of North Carolina's own experience is needed in an effort to assess the

effect of changes in tort law upon the costs and availability of liability insurance in North Carolina.

Careful study is needed to determine whether North Carolina loss experience provides the basis for the costs and availability problems encountered in North Carolina.

To the extent that North Carolina premium rates are based upon national loss experience or are affected by significant levels of reinsurance, the impact of changes in North Carolina tort law alone upon the cost and availability of insurance in the state is likely to be diminished. Some observers believe that, in the context of tort law developments across the nation in the past few decades, North Carolina tort law has remained conservative and that North Carolina's loss experience is modest in comparison to that of many states. These observers question whether, if savings could be effected through changes in tort law of North Carolina, those savings would appreciably improve the cost or availability of liability insurance in North Carolina. These observations need to be tested. If the difficulties encountered reflect North Carolina loss experience, careful consideration of factors that will improve the North Carolina experience may be needed. On the other hand, if the difficulties are not primarily a result of the North Carolina experience, careful consideration of cost and availability of liability insurance in the state may be needed. For example, the possibility of implementing the North Carolina

Health Care Excess Liability Fund for this purpose may need to be examined.

Careful study is needed to evaluate the fairness of the present tort system as well as the proposals for change in it.

Everyone agrees that basic fairness is essential to the tort system. Substantially conflicting views exist about what is needed to achieve fairness.

Here, more so than in other areas, views tend to be much more emotional. One view holds that recovery for pain and suffering is totally unjustified, jury verdicts are clearly excessive, and greedy clients and lawyers stir up frivolous suits. It is largely changes to limit damages for pain and suffering, to place caps on overall damage recoveries, and to eliminate the collateral source rule. If these underlying assumptions are correct, the recommended changes in tort law would offset the perceived windfalls. If the underlying assumptions are erroneous, however, the changes would deprive injured persons of reasonable compensation. Further, uncertainty exists about the dollar value of the "windfall" arising if the assumptions are correct or the "deprivation" caused if the assumptions are erroneous. These issues, of course, cannot be resolved without further study. But until careful study permits some meaningful resolution of them, fundamental change in the tort law is at best haphazard.

Questions have been raised about the fairness of the attorney's contingent fee which in many cases results in payment

to the attorney of a substantial part of the injured person's recovery. A satisfactory solution, however, will not necessarily be forthcoming if focus is limited to this one dimension and no consideration is given to possible adverse effects upon the injured person's ability to obtain good legal representation and the impact of such representation on his success in pursuing claims against tortfeasors. Only if all relevant factors are considered can a workable solution be found.

Some means to screen out frivolous suits is desirable. The large percentage of malpractice claims that are unsuccessful suggests that both fairness and efficiency could be promoted by an effective screening mechanism. Possible alternative solutions should be identified and studied in an effort to find a solution that would not severely limit the longstanding policy of free access to the courts that is part of this State's traditions.

FEDERAL TASK FORCE ON TORT REFORM POSITION²

Recent legal movements by activist judges and tort lawyers who see no bounds to the ever increasing expansion of tort liability have caused the crisis. These judges and lawyers have become dissatisfied with using tort law as a means to deter undesirable conduct and now want to use it as a vehicle to restructure society and administer a massive social insurance scheme. The following are a few of the major problems facing the tort system and some possible causes and solutions.

The first of the problems is the movement toward no-fault liability. Traditionally, tort law punishes those who have done wrong by making them compensate those whom they have wronged. But increasingly, tort law now punishes those who have done nothing wrong, simply because they often have the resources to compensate the unfortunate. This trend is especially pronounced in the expansion of strict liability doctrines in the areas of design defect and failure to warn. Strict product liability in its

²This is derived from a speech given by Richard K. Willard, Assistant U.S. Attorney General, Civil Division, before the American Consulting Engineers council concerning the current liability insurance "crisis" and from an article that appeared in The Legal System Assault on the Economy--Volume III, a publication of the National Legal Center for the Public Interest, published in October, 1986. Mr. Willard was Counsel to the Federal Task Force on Tort Reform created by President Reagan to determine the Federal response to the liability insurance "crisis." After presenting the statistical background for the problem, he went on to discuss the causes of the "crisis" and proposed solutions.

traditional form is a fault-based system of liability, although the standard of fault is more generous to the plaintiff than common law negligence. A "fault-based" system is one that only permits recovery where the defendant has engaged in an activity that society deems harmful and wishes to deter. The negligence standard used in other tort areas is one way of ascertaining whether an activity falls within that category. Strict liability uses different mechanisms for making that determination in light of the realities of modern industrialized life.

Used in the right situation, strict liability is a useful tool. However, over-zealous application of strict liability principles in areas where such principles were never intended to be applied has resulted in numerous damage awards by juries that would have been rejected under any reasonable interpretation of a liability standard.

Further complicating the standard of strict liability is the acceptance by courts of liability without a showing of causation. In other words, irrespective of the factual basis of the claim and even in the presence of contradictory evidence, a mere assertion that a product cause an injury is enough to obtain money from its manufacturer. As farfetched as such a standard may seem, a number of recent lawsuits seem to be moving in this direction. The trend towards liability without fault or proof of causation is based upon emotionalism and an unprincipled willingness to award recoveries against "deep pocket" defendants.

The trend towards making defendants liable for risks that are practically impossible to discern or protect against should be cause of great concern. Potential liability becomes astronomical and entirely incalculable. Insurance companies calculate rates according to risk projections. They charge premiums that will allow them to absorb a projected amount of legitimate claims. Of necessity, they base their projections upon the assumption that claims are legitimate only when an insured has been found to be at fault. Without a fault-based system, insurance companies are not able to calculate with reasonable accuracy the amounts for which their insureds will be held liable and they will not offer coverage.

Instead of continuing on this destructive path, we should return to a view of tort law premised on the concept of fault. Fault is not some archaic vestige of tort law to be jettisoned whenever it stands in the way of compensation. Ultimately, it is the only reliable vehicle for distinguishing socially beneficial from socially harmful conduct and activities.

A second problem in the development of the tort law system is the extraordinary increase in the size of awards. The prospect of large awards provides a strong incentive for individuals to sue, and it also inflates the size of initial damage claims. The most troubling aspect of this development is that much of it has come in the form of noneconomic damages such as pain and suffering or mental anguish and punitive damages. Such damages are inherently

unconstrained, and in recent years have resulted in some staggering awards. Another remarkable development in tort actions between private parties is that awards of punitive damages have increased dramatically. Punitive damages were originally intended to punish particularly egregious or malicious conduct. Such damages may have a place in a system based on fault. One would therefore expect that as the tort system moved away from fault, punitive damage awards would become rarer. Instead, the incidence and size of punitive awards seems to be increasing. If this trend towards massive increases in punitive and noneconomic damages continues, its impact on the economy of this nation is likely to be devastating.

The intellectual force driving this expansion of tort law is the desire to provide benefits to the unfortunate. But the primary beneficiaries of expanded tort liability have been the lawyers. One of the most controversial areas in tort cases is the extent to which damage awards are absorbed by attorney's contingency fees. Attorney's fees frequently amount to one-third to one-half of any award granted by the jury.

What should be done then? Unfortunately many would simply create more government programs to assume the liability burdens of those interests which cannot function under current conditions. This problem must be attacked at its root by seeking reform of the tort law system. An important element of tort reform is to keep damage awards proportional to economic loss by placing a cap on

awards for noneconomic damages. In California, a \$250,000 cap has been applied to awards for noneconomic losses in medical malpractice cases. The United States Supreme Court refused to hear a challenge to the constitutionality of the California statute. This opens the door for other states to adopt a similar approach in all tort cases to limit noneconomic damages so that risk can be more easily evaluated and insured.

The intangible injuries do exist, but it is necessary to recognize that the valuation of damages resulting from them is a subjective determination. Such subjective decisions are better based on standards developed by an elected legislature answerable to the public, than turned over to juries easily swayed by emotional arguments of attorneys with an incentive to inflate damage awards to the greatest extent possible.

It is important to keep in mind that the crisis of the tort system has been developing over many years and has many aspects. There is no panacea. The state and federal courts, the Congress, and the state legislatures must work together to deal with this crisis effectively.

* * * * *

IS THERE A LITIGATION EXPLOSION?

In recent weeks, however, some people have begun to raise the question of whether there is indeed a litigation explosion. The April 21 issue of Business Week magazine and the April 28 issue of the National Law Journal, for example, cite a new study by the

National Center for State Courts. That report finds that tort lawsuits filed in selected courts in selected states from 1978 to 1984 increased by nine percent, as compared to an eight percent population increase during this same period. On the basis of this, the report concludes that there is no "litigation explosion"--at least not in recent years.

The conclusion of the report, while perhaps technically correct, provides us with an excellent example of how the improper use of statistics can prove highly misleading in the context of the current tort reform debate. Putting aside any questions concerning the methodology used in the study, the Center's report is fundamentally misleading for a very simple reason: it fails to account separately for automobile accident related lawsuits.

Automobile accidents are involved in one-half to two-thirds of all tort filings. Any decrease in automobile cases, therefore, can readily offset major increases in the types of cases at the core of the tort reform debate--product liability, medical malpractice, professional liability, and municipal liability.

The decrease in the number of automobile related lawsuits is easily understood when one considers two developments over the past several years. First, for a variety of reasons--the 55 mph speed limit, safer cars, harsher drunk driving penalties, higher gasoline prices--the number of automobile related injuries has been decreasing. A second factor leading to the decrease in

automobile accident lawsuits is the development of no-fault automobile liability insurance.

The fact that such decreases in automobile related lawsuits can readily conceal significant increases in product and professional liability filings is easily demonstrated by reviewing data on filings in federal courts. Tort actions in federal court increased from 24,231 in 1974 to 41,593 in 1985, a 72 percent increase. Product liability actions in this same period, however, increased by 1,579 to 13,554, a 758 percent increase. Likewise, medical malpractice cases increased from 385 in 1978 to 1,779 in 1985 a 362 percent increase. Thus, one would arrive at a very different conclusion from looking specifically at the problem areas of product liability or medical malpractice, than from looking only at tort filings generally.

By properly examining the relevant data, we can easily see that the litigation explosion is not a myth, but reality. In particular, the explosion of litigation and expansion of liability in certain types of cases is directly correlated with the crisis in the availability and affordability of those types of liability insurance.

* * * * *

THE REAGAN ADMINISTRATION'S LEGISLATIVE PACKAGE

Attorney General Meese and Commerce Secretary Baldridge announced the Reagan administration's support for three federal legislative proposals for tort reform. The specific provisions of

these bills are based on the recommendations of the Tort Policy Working Group, contained in the February 1986 report.

The first legislative proposal is the Product Liability Reform Act of 1986. This bill contains provisions that will:

- require liability to be based on fault;
- limit application of the doctrine of joint liability to those situations where the defendants have acted in concert;
- place a cap of \$100,000 on the amount of noneconomic damages--such as pain and suffering, mental anguish, and punitive damages--that can be awarded;
- provide for future economic damages to be paid in periodic installments;
- modify collateral compensation doctrines to eliminate double recovery by plaintiffs;
- encourage states to develop and use alternative dispute resolution mechanisms that will help alleviate burgeoning caseloads in the courts and allow injured parties to receive a greater share of any award in a more timely fashion; and
- Alleviate the excessive transaction costs of our tort system by placing reasonable limits on contingency fees charged by attorneys.

The bill will assist those American businesses, particularly small businesses, that are unable to obtain reasonably affordable

insurance because of the high costs of the current liability system. Of course, the ultimate effect of all this will be to benefit consumers by lowering prices, and where injury is caused by the negligence of another, the injured party will receive a greater share of the damages and in a quicker fashion than if that party had to rely on the current legal system.

The second piece of legislation is the Government Contractor Liability Reform Act of 1986. This act will extend the product liability provisions outlined above to government contractors. Separate legislation to protect government contractors is necessary to ensure that the United States can obtain at a reasonable cost the goods and services necessary to further the public welfare.

The last bill is the Federal Tort Claims Reform Act of 1986, which contains provisions that, with few exceptions, are identical to the product liability reform legislation. Those provisions are made specifically applicable to the tort liability of the United States, thereby benefiting the American taxpayer who's federal tax dollars must satisfy every judgment against the government.

These legislative reforms are just a beginning, and to be effective, they must be accompanied by similar undertakings at the state level. These efforts will begin to correct the worst abuses of our present liability system. Enactment of these reforms at the federal and state levels will return our civil liability doctrines to fair and fault based standards designed to compensate

the injured party. They will also provide a beneficial impact not only for the business community, but, more importantly, for consumers.

BUSINESS POSITION AS EXPRESSED IN FORBES MAGAZINE³

In 1984 the average product liability award in the United States was \$1.07 million--up from \$345,000 ten years earlier--and the average medical malpractice award was \$950,000. In 1983 there were 360 personal-injury cases settled with million-dollar awards or more, thirteen times the number settled for that amount in 1975. In 1984 there was one private civil lawsuit filed for every 15 Americans. An estimated 16.6 million civil suits were tried in state courts last year. Another 150,000 private civil suits were tried in federal courts, which is nearly twice the number ten years ago.

In 1984 the property and casualty insurance industry as a whole paid out \$116.10 for every \$100 received in premiums. Reinsurers, who take the brunt of the unpredictable risks, paid out nearly \$141 for every \$100 in premium income.

No industry can keep up those payments in excess of income up for long. Courts have expanded the definitions of liability to such an extent that some companies have decided not to sell liability insurance. The flight of insurers and reinsurers is most visible where the risks of winding up on a courtroom are

³Another view, typical of what the Commission heard from business during its deliberations, concerning the liability marketing situation was in a lengthy Forbes Magazine article, first published on July 15, 1985, from which this information is taken.

great--both gradual and sudden-and-accidental pollution, directors' liability, municipal liability, medical malpractice, and accountants' liability.

Property and casualty insurance has always been a boom and bust business, but the bust has never been this bad. Blame part of it on greed. After five years of cash-flow underwriting--pricing products at a loss in underwriting terms in order to bring in extra dollars to invest at high interest rates--the industry has hit rock-bottom. In 1984 it recorded a pretax loss of \$3.8 billion.

There's no way that the insurance industry can fully recover from its current downswing until Congress--or state legislatures--step in and impose order on our self-destructive legal system. Pennsylvania has already made a start with legislation that curbs pain and suffering awards from municipalities.

In the meantime, property and casualty insurance is going to become much tougher to get, at any price. By far the most common strategy is to accept limits on coverage--higher deductibles, lower protection levels and, increasingly, exclusions for items such as legal defense costs and pollution liability.

Insurers have also started pushing "claims-made" policies, which pay off only those claims filed during the policy term. Supporters of these policies argue that they will help insurers define their legal risks better and thus enable them to keep selling the product.

The last resort is self-insurance, either setting up a reserve fund to cover uninsured costs or paying them out of operating expenses. Some companies are setting up insurance captives, as they did in the mid-1970's. Captives are not very attractive from a tax standpoint and they are risky. Some see self-insurance as a curb on litigation. Self-insurance carries the risk of being pushed into Chapter 11 bankruptcy.

Industry insurance pools are popular with utilities, lawyers, accountants, fuel distributors and others. The exposure for any insurer of a single high-risk industry is enormous, even when only claims-made policies are sold. So some companies try to spread their risk by setting up multi-industry insurance pools with the same problems as commercial insurers.

The problem cannot be dealt with solely from the insurance side of the equation. It must be approached from the legal side. As long as judges keep expanding the definition of liability and juries keep returning extremely high awards, the prospect of a total withdrawal of commercial insurers from the liability and property insurance lines exists.

Perhaps the only practical solution is legislative action to define liabilities and cap them at a fair and reasonable level. Congress has contemplated a proposal that would put a limit on corporate liabilities.

AMERICAN TRIAL LAWYERS ASSOCIATION POSITION⁴

"When a fox is marauding through the henhouses, people don't usually blame the chickens. Yet that's what's happening in the insurance crisis today.

"Let's not be fooled. The insurance industry is a very smart fox indeed. Let's look at just how foxy the insurance companies are.

"'The tort system is destroying me,' they cry, asking us to ignore these facts:

"(1) In 1985, the property and casualty industry's net worth rose by \$7.6 billion! Who else can lose money and watch its net worth increase? (Source: A.M. Best Review & Preview 1986)

"(2) The industry's stocks outperformed the market by 100 percent in 1985, and, over the last 10 years, the leading property and casualty stocks rose by 500 percent, more than double the increase in the Dow Jones Industrial Average. (Investors and shareholders are told one story, and the insureds are told another.)

⁴This is typical of the information that the Commission received from trial lawyers and persons representing consumer organizations and was taken from the President's Page from the April, 1986 issue of Trial, a publication of the American Trial Lawyers Association, which contained the comments of Peter Perlman, President of that organization.

"(3) The industry's fourth-quarter profits were up an incredible 881 percent over 1984--poor fox! (U.S.A. Today, January 4, 1986)

"(4) 'The property and casualty industry to day is in a stronger capital and surplus position that it has ever been in...' (National Underwriter, November 8, 1985)

"Rather than blaming innocent victims or juries, judges, and lawyers, it's time insurers did some soul searching. Let's consider a few of the industry sources:

"(1) 'The property/casualty industry must accept major responsibility for its current financial condition.' (Insurance Services Offices of the National Association of Independent Insurers, 1985--A Critical Year)

"(2) The price wars of the previous decade certainly were not started by consumers. 'Interest rates were near 20 percent and the companies were begging for business at any price to get premium dollars to invest.' (New York Times, October 20, 1985)

"This new 'crisis' is like the 'crisis' of the mid-70s, which the Department of Commerce called 'not a crisis at all, but overly subjective rate-making.' (U.S. Department of Commerce, Product Liability and Accident Compensation Task Force, Report on Product Liability Ratemaking(1980).

"When interest rates were high, the hungry old fox saw a way to get fat on investment income, by slashing premiums in a thoughtless and irresponsible manner."

"Under the McCarran/Ferguson Act, the insurance industry is exempt from the federal antitrust laws--the only major industry in the country to get this kind of special treatment....The insurers have set doctors, mayors, day care center owners, tavern keepers, business proprietors, and even Girl Scout Troop leaders at the throats of the lawyers and juries, and while everyone else is watching the fight, the insurance industry is busy picking all of our pockets."

"Let's take a closer look at these cunning creatures. With a flick of the wrist, they manipulate reserves to show whatever is to their advantage. In spite of this, the industry reported a profit of \$72 billion for the decade ending in 1983. Did the insurers pay their fair share of taxes? They paid 2 percent of their profits--\$1.3 billion. (Source: U.S. General Accounting Office)

"The insurance industry is not an endangered species but a predator. It's time to revoke the special treatments and insist that corporations that sell insurance are just like any other corporations:

"**Insurers should pay a fair and reasonable amount of federal, state and local tax--in other words, they should be held to the same standards of citizenship as other corporations.

"**Insurers should no longer have their special exemption from the antitrust laws.

"**State regulators should regulate. Before allowing any rate hikes or and discontinuance of lines, they should require the insurance industry to provide them with full historical information on payouts (not just reserves, on which the companies can keep earning income, but actual payouts) and require that investment income be considered as well as premium income in setting rates (after all, the capital that's invested comes from premium income, doesn't it?)

"**Insurance companies should experience-rate their clients. Insurers can be a force for safety by making things tougher on those who cause more problems. Insurers experience-rate drivers; why not doctors, or lawyers, or other professionals who cause disproportionate amounts of harm--and claims?

"**Insurance companies should look at their own management practices instead of asking consumers to fund their mistakes. 'A mindless price war brought the property/casualty business to its low and sorry state.' (Journal of Commerce, June 20, 1985)

"**Courts should require prejudgment interest to help convince insurers to bargain in good faith. If they were already doing that, the tort of bad faith would never have developed. But it's there, and it must be discouraged."

THE CONSUMERIST'S POSITION⁵

"In state after state, doctors, lawyers, accountants, hospitals, daycare centers, school districts, directors and officers of corporations, municipal, county, and state governments, and a wide variety of other economic enterprises report massive premium increases, midterm changes in contract terms, policy renewal rejections, and an inability to find liability insurance at any price.

"State governments have addressed this problem by imposing emergency rules and creating commissions to investigate the issue and propose solutions....

"Unfortunately, the debate and policy proposals to alleviate the liability insurance crisis have focused on only one aspect of the problem: possible deficiencies in the tort system. In particular, the 'quick-fix' that seems to be gaining favor emphasizes limitations on victims' rights to recover damages. Liability limits, caps on noneconomic damages, changes in the statute of limitations for lawsuits, and other changes have become the centerpieces of the recommendations of many state task forces.

"Ignored in this 'rush to judgment' is a part of the problem far more important than anything happening in the nation's

⁵In the April, 1986 issue of Trial is an article by J. Robert Hunter, President of the National Insurance Consumer Organization, which represents this consumerist position of the liability insurance "crisis."

courtrooms: The way the insurance industry routinely conducts business. Our initial analysis of the problem leads us to conclude that if industry practices could be modified by enhanced regulatory vigilance, the part of the problem to be solved by tort reform would be small indeed. We believe the liability insurance crisis is primarily an insurance problem.

"The primary reason for this crisis has so suddenly materialized is that the insurance industry practices 'cash-flow underwriting.' When interest rates and investment returns are high, insurance companies accept riskier exposures to acquire more investable premium and loss reserves....Ultimately, of course, losses had to be paid. When those losses corresponded with the declining interest rates and investment yields of the past two years, companies attempted to both raise premiums and shed themselves of riskier business lines to maintain their earnings....The result of this cyclical behavior is instability in the market: When interest rates and investment income are high, companies offer riskier coverages at discount prices, but when the consequent losses must be paid and interest rates and investment income drop, they increase premiums dramatically and cancel certain exposures regardless of price.

"We see today's crisis as a repeat performance of the liability insurance crisis of the mid-1970s, a crisis that followed a similar period of very high interest rates and rapid decline. Just as is the case today, the industry pointed to the

courts as the primary culprit and secured a number of 'tort reforms' in state legislatures. Yet, 10 years later, the problem is back damaging state economies, reducing the supply of necessary business and governmental services, and causing economic disruption in state after state.

"Our analysis leads us to conclude that tort reform is no panacea for the liability insurance crisis. Improved regulatory control over insurer costs and rates is what is needed. Significant changes in interest rates are a routine part of our economic landscape....In setting rates, property/casualty insurers seldom document their claimed operating expenses. Rather they simply allocate these costs between insurance lines and states in proportion to premiums. Moreover, there is little if any regulatory attention to the appropriateness of specific expense items....States should more carefully examine both the level and allocation of insurance company expenses as a part of the rate review and approval process....

"It is possible the industry is simply 'going out on strike,' exaggerating its financial position to pressure legislators into creating a lower risk environment for their operations....

"The primary cause of the liability insurance crisis is not to be found in our legal system; tort reform is not all that will be required to solve it. Our analysis indicates that attention must be given to both the regulatory and the tort side of the problem in order to craft a sensible response to the problem.

"Before states further reduce victims' rights with liability limits, caps, and other quick fixes, they should identify and correct the part of the problem caused by insurance industry practice. They should first start by getting the insurers' closed claims to see how victims are faring under the current system and then see how much money, if any, consumers would save if caps and other so-called reforms were enacted.

THE FREQUENCY AND SEVERITY OF MEDICAL MALPRACTICE CLAIMS: NEW EVIDENCE.⁶

Physicians have been liable for medical malpractice since the eighteenth century in the United States, but malpractice claims were rare until recently. In the late 1960's the frequency of claims per physician and claim severity (size of the award per paid claim) began to increase at unprecedented rates, culminating in the medical malpractice "crisis" of the mid-1970's. In response to this crisis, legislatures in almost every state enacted tort reforms intended to curb the rise in claims, in addition to other changes designed to assure the availability of malpractice insurance.

Between 1975 and 1978, claim frequency per physician slowed or even decreased in many states, but since 1978 claim frequency has resumed an upward trend.

To date, there have been only two published statistical analyses of the impact of tort reforms and other factors on malpractice claims. My earlier analysis of tort claims during the 1970's concluded that the increase in claims over time and the persistent diversity in experience among states could only partly

⁶The following are excerpts from an article by Patricia M. Danzon, Associate Professor of Health Care Systems and Insurance, University of Pennsylvania which was reprinted in Law and Contemporary Problems, Vol 49, #2, Spring 1986. The article describes a detailed statistical analysis of the results of tort reforms as relates to medical malpractice cases. It is arguable that the same results would apply to tort cases other than medical malpractice cases that result in personal injury and property damage.

be explained by such factors as the increase in the number and complexity of medical treatments and the concomitant increase in the exposure to the risk of iatrogenic⁷injury. The plaintiff trend in common law during the 1950's and 1960's also appears to have contributed significantly to the rise in claim frequency and severity. The other major factor contributing to the diversity among states was urbanization; however, the specific characteristics of urban environments that generate higher frequency and severity could not be identified. Difference in the number of attorneys per capita, the cost of medical services, per capita income, and unemployment rates did not appear to play a significant role.

This early analysis found mixed effects of the tort reforms enacted in response to the 1975 crisis. Limitations on the plaintiff's recovery (caps on awards) and mandatory offset of collateral benefits appear, by 1978, to have significantly slowed the growth of claim severity in states that enacted such changes. However, none of the other changes, such as pre-trial screening panels or shorter statutes of limitations showed any impact on frequency or severity. Moreover, none of the reforms could explain, in a statistical sense, the lull in growth of claim frequency that occurred between 1975 and 1978. However, this early analysis, using data on claims closed through 1978, obviously did not purport to measure the long-run impact of the

⁷Ed. note. "iatrogenic injury" is defined as injury caused by medical treatment.

tort reforms enacted since 1975. In particular, any impact of shorter statutes of limitations on the "long tail" of claims would not have been evident. Even the estimates of the apparent short-run effects might have been contaminated by other unmeasured factors related to the crisis, such as changes in public attitudes, which might prove short-lived.

Given the recent rise in claims and severity as well as the necessarily less-than-definitive nature of previous analyses, the time is ripe for additional information. The study reported here updates the earlier estimates of how tort reforms and other factors have affected trends in malpractice claim frequency and severity, using nationwide claims experience over the full decade 1975 through 1984. The length of time since the enactment of the 1975-1976 tort reforms should, in principle, now be long enough to estimate their long-run impact. However, in practice several difficulties remain. First the reforms have been subject to legal challenge in many states, and final rulings on their validity have been long delayed. To the extent that the disposition of malpractice claims over the last decade has been influenced by uncertainty as to ultimate judicial outcomes, it may still be too early to estimate the full long-run effects of those reforms that have been upheld.

A second practical difficulty is the lack of a consistent and comprehensive data base.

The following report on malpractice claims begins with a brief description of the data base and methodological issues which are covered in more detail in the appendix. The next section analyzes the frequency of claims filed and claims closed with payment. Trends in malpractice claims severity are then analyzed. The concluding section summarizes the findings of the report.⁸

* * * * *

3. Non-Tort Sanctions. Since 1975 many states have strengthened their procedures for quality control through medical quality assurance boards, partly as a quid pro quo for tort reform. In theory, the amount of malpractice claims should be lower in states with active disciplinary boards. Contrary to this expectation, claim frequency tended to be positively related to the number of disciplinary procedures per 1,000 physicians, but statistical significance levels were low. This finding suggests that disciplinary procedures are tightened in states experiencing high claim frequency.

4. Urbanization. My earlier analysis concluded that urbanization was the single most important factor contributing to interstate differences in malpractice claims. The results here tend to confirm that conclusion, with qualifications.

5. The Business Cycle. It is often argued that personal injury and disability claims are inversely related to the business

⁸A copy of the full article has been filed with the minutes of the Commission and is available for review in the legislative library.

cycle. A plausible reason might be that when business activity is low and unemployment rates are high, the opportunity cost of time for attorneys and patients is low. Moreover, plaintiffs are less likely to have first-party insurance coverage through their employers, so they may be more willing to seek compensation through the tort system. The evidence here is inconsistent with this hypothesis.

6. The Doctor-Patient Relationship. The rise in malpractice claims and the high incidence of claims in urban areas are often attributed to the erosion of traditional long-standing physician-patient relationships with a family physician, which, it is argued, constituted a psychological barrier to suit. Contrary to these hypotheses, population turnover has no systematic impact except for late-filed claims, where the impact is negative.

7. The Elderly. Consistent with my earlier analysis, these data show no relationship between claim frequency and the percentage of the population over sixty-five, so this variable is omitted from the reported equations.

8. Number of Lawyers. Also consistent with my earlier analysis, there is no evidence that a high density of lawyers per capita has any systematic impact on the frequency of claims filed, after controlling for other characteristics of areas with high lawyer density.

C. TORT REFORMS

In evaluating the evidence on the impact of tort reforms, it must be emphasized that there is some uncertainty as to the true levels of statistical significance because of the limitations of the data. The following results only show how much a particular reform affected experience relative to what that experience would have been had the law not been enacted.

1. Statute of Limitations. States that have enacted shorter statutes of limitations have experienced some reduction in claim frequency. Reducing the statute of limitations for adults by one year reduces the total claim frequency by eight percent and frequency of paid claims by six to seven percent.

2. Collateral Benefits. The only other reforms that show any evidence of reducing claim frequency are laws that permit or mandate reducing awards by the amount of insurance coverage from other sources. Collateral source offset is estimated to reduce claim frequency by fourteen percent.

IV

TRENDS IN MALPRACTICE CLAIMS SEVERITY

A. Theoretical Model of Claim Severity

In theory, average severity is expected to depend on the "true" damages incurred on claims closed with payment and on the valuation of these damages by the courts. "True" damages depend on the mix of injury severity in the sample of claims receiving payment and on the plaintiffs' actual or potential wage loss,

medical expenses, and noneconomic loss. In principle, the rules of compensable damages determine the valuation of these damages by the courts, subject to interpretation by the judge and jury. Whether changes in these rules have any impact in practice is one of the empirical questions being addressed here.

Of the post-1975 tort reforms, those most directly aimed at reducing severity are caps on awards (either on the total award or, more commonly, on the component of pain and suffering), modification of the collateral source rule (to admit evidence or mandate offset of compensation from other sources), and provisions for periodic payment of future damages. Ceilings or schedules for contingent fees may also reduce awards to the extent that they are enforceable and reduce the incentives of plaintiff attorneys to pursue claims. Although caps on awards and sliding-scale fee ceilings are most likely to affect very large potential awards, which are a small fraction of all claims, these few cases account for a very large fraction of the dollars paid. Therefore, they can substantially influence average severity.

Reducing awards is also one objective of arbitration proponents, since eliminating the role of the supposedly overgenerous jury is one of the major differences between arbitration and tort procedure. Finally, screening panels may affect potential severity, to the extent that panels change the cost of litigation or have direct power to determine damages. Panels may also indirectly affect observed severity to the extent

that they screen out "frivolous" claims that might otherwise have been settled with a small payment. By so doing, panels may change the mix of claims paid and raise the average amount actually received.

B. FINDINGS

1. Time Trend. Malpractice claim severity has risen roughly twice as fast as the Consumer Price Index (CPI). As noted above, this growth in average severity may underestimate the growth in "generosity" of the tort system, to the extent that the potential for more generous awards induces the filing of more minor claims.

2. Urbanization. Consistent with the findings of my earlier study, claim severity is significantly higher in urbanized areas.

Claim severity also is significantly higher in states with a high ratio of surgical specialists relative to medical specialists. This variable may capture the general effect of more complex medical practice, as well as the likelihood that surgical mishaps involve more serious injuries and are easier to prove.

3. The Elderly. As expected, average severity is lower in the states with a relatively large elderly population in view of the lower compensable damages for the elderly. However, the level of statistical significance is low.

4. Number of Lawyers. There is no evidence that the number of lawyers per capita has any impact on claim severity.

C. Tort Reforms

The estimates of the impact of tort reforms are reasonably consistent with theory and with the earlier findings.

1. Caps on Awards. The average impact on the various statutes to cap all or part of the plaintiff's recovery has been to reduce average severity by twenty-three percent. This observed average impact obviously masks great differences among cases. The majority of cases would be unaffected by most of the caps. Therefore, the impact on the few large awards that are affected must be substantially greater than the average over all cases. Because large awards count for a disproportionate fraction of total dollars (over fifty percent of dollars are paid on five percent of cases) caps that severely reduce the few very large dollar awards can have a significant impact on the average and on the total payout.

2. Collateral Source Offset. Laws providing for collateral source offset appear to reduce awards between eleven and eighteen percent.

3. Arbitration. States that have enacted special statutes permitting voluntary binding arbitration have an average claim severity roughly twenty percent lower than other states.

V

CONCLUSION

The tort reforms enacted since the mid-1970's malpractice "crisis" affected the frequency and severity of malpractice claims

over the decade from 1975 to 1984 in a manner broadly consistent with economic theory and with previous evidence. Although claim frequency and severity have continued to rise despite reforms, this trend does not indicate that the tort changes have had no effect. States that enacted shorter statutes of limitations and set outer limits on discovery rules have had less growth in claims frequency than states with statutes more lenient to the plaintiffs. On average, cutting one year off the statute of limitations for adults reduces claim frequency by eight percent. The effect would presumably be greater for a reduction from, say, four to three years than from ten to nine years. (Percentage changes are the average differential in a single year, relative to what the situation would have been without enactment of the reform.)

Statutes permitting or mandating the offset of collateral benefits have apparently reduced malpractice claims severity by eleven to eighteen percent and claim frequency by fourteen percent relative to comparable states without collateral source offset. The feedback from a reduction in severity to a reduction in frequency is not surprising, since collateral source offset reduces the potential recovery for a large number of claims, thereby reducing incentives to file.

Caps on awards have reduced severity by twenty-three percent. This percentage represents the average impact of the various forms of cap, over the period of 1975 to 1984, during which time some

statutes were still under challenge. If the dollar thresholds are not revised periodically to keep pace with inflation, the future effect will presumably be greater, unless juries find ways of implicitly circumventing the limits by increasing allowances for uncapped components of the award.

Arbitration statutes apparently increased claim frequency, but reduced overall average severity. Disaggregated data would be necessary to determine whether the reduction in observed average severity results from reduction in awards per case or simply reflects the filing of more small claims. The net effect appears to be an increase in total claim costs, but compensation of more claimants.

None of the other reforms analyzed, including screening panels and limits of contingent fees, appear to have had any systematic impact on claim frequency or severity.

An overall evaluation of the merits of the various tort reforms from a public policy perspective is beyond the scope of this paper and has been done elsewhere. However, it is worth noting that on average, severity has increased at almost twice the rate of inflation of consumer prices over the last decade. Thus, in the absence of further statutory controls, the income of successful malpractice claimants--or at least some of them--will continue to rise relative to the income of the population as a whole, and relative to the income of other accident victims who

are not compensated through the tort system. The optimal structure of tort awards therefore warrants further attention.

And beyond the scope of this paper is the impact--actual or potential--of tort reforms on malpractice insurance premiums. The analysis here of impact on claim frequency and severity should not automatically be translated into an effect on premiums for several reasons. First, the net potential impact on premiums also depends on litigation expenses and changes in the timing of disbursement of loss reserves, and hence investment income. Second, reforms that reduce the uncertainty in estimating malpractice claim costs--namely, caps on awards, periodic payment of amounts for future damages, and shorter statutes of repose (running from the date of incident, not date of discovery)--may be expected to reduce premiums by a modest amount, over and above the reduction in mean expected losses. One can expect this result because of the reduction in the insurers' risk. Perhaps more importantly, by reducing uncertainty, such reforms should reduce the volatility in price and availability of malpractice insurance, which is a major inefficiency of the present malpractice system.

COMMISSION PROCEEDINGS

The Liability and Property Insurance Markets Study Commission was created by House Bill 344 which was enacted as Chapter 792 of the 1985 Session Laws (See Appendix C for this legislation). The Commission was directed to study:

- "(a) The availability of professional and commercial liability and property insurance in this State and the factors causing and compounding diminutions in underwriting capacity.
- (b) The underwriting and marketing practices of admitted and nonadmitted liability and property insurers and producers doing business in this State.
- (c) Optional methods of risk management and risk sharing that may be utilized by the citizens of this State.
- (d) The effect of diminished underwriting capacity in professional and commercial liability and property insurance on the economy of this State.
- (e) Any other subjects deemed by the Commission to be relevant to this study."

The Commission was appointed by the Speaker of the House of Representatives, the President of the Senate, and the Commissioner of Insurance, in accordance with the enabling legislation (See Appendix D for a list of the Commission membership.) and met for the first time in Raleigh on October 22, 1985. The Commission conducted four public hearings across the state, in Kinston (on

November 13, 1985), Laurinburg (on November 14, 1985), Asheville (on December 4, 1985), and Charlotte (on December 5, 1985), at which members of the public were invited to make presentations to the Commission. The Commission heard from representatives of the insurance industry, insurance agents, the general business community, municipalities, counties, and the public at-large (See Appendix E for a list of the persons making presentations at the various public hearings.)

The Commission continued its deliberations with an additional public hearing in Raleigh on February 3, 1986. Prior to this last scheduled public hearing, the Commission notified all interested parties that this would be the last public hearing and that after this meeting, speakers would be allowed to address the Commission by invitation only. (See Appendix F for a list of persons or organization that received copies of all mailings from the Commission.)

The Insurance Industry was asked to provide "high-ranking" spokesmen from several insurance companies who could answer Commission questions concerning the companies' market strategies and what legislation would be required to bring the companies back into the North Carolina market. One regional manager from one insurance company spoke for the insurance industry.

It was during this public hearing that the Commissioner of Insurance, James E. Long, announced that he had asked Governor Martin to call a special session of the General Assembly to

consider giving him stand-by authority to compel the insurance industry to provide critically needed but unavailable insurance coverages. The Commission strongly supported the call for the special session and the legislative members of the Commission worked for the passage of the legislation proposed by the Commissioner of Insurance.

After the special session the Cochairmen of the Commission sent a notice to the Commission members indicating that, while the legislation passed by the General Assembly in its February special session was an attempt to address the problems of unavailability of insurance, the legislation that was passed did nothing to address the problems of affordability and extent of coverage of liability insurance offered in the North Carolina market.

The Commission met in Raleigh on April 1, 1986 and divided into two subcommittees, one on insurance regulation and one on civil justice modification, to continue its deliberations. These subcommittees considered more than forty proposed solutions to the perceived liability insurance problems derived from the presentations at the public hearings, the literature received by the Commission, the results of a survey conducted to determine the actions taken or proposed in other states, and many other sources.

The "Potential Solutions List" that follows was the list considered by the Commission.

POTENTIAL SOLUTIONS LIST

Local Governments

Authorize Insurance Pooling

Local Government Tort Claims Act

Expand Sovereign Immunity to Shield Local Governments Against
Suits

Define "Governmental" and "Proprietary" Functions

Limit Claims Against Local Governments

Professionals

Eliminate or Modify Joint and Several Liability

Shortening Statutes of Limitations

Statutory Language Limiting Judgments to "State of Art" at Time of
Design, Infraction, or Injury

Amending Workmen's Compensation Law to Include "Design
Professionals" Within Immunity Afforded to Employers

Require Second Opinion From Professional Before Allowing Lawsuit
to be Filed

Civil Justice Reform

Caps on Noneconomic Damages

Prescreening of Liability Lawsuits

Mandatory Arbitration

"Blue Ribbon" Professional Juries to Determine Liability and
Damages

Binding Arbitration of Liability Claims

Limiting Contingency Fee Contracts Between Lawyers and Clients

Elimination or Limitation of Punitive Damages

Punitive Damages Going to State or Charitable Interests

Shortening Statutes of Limitations

Notice of Intent to Sue Within Statute of Limitations

Definition of "Gross Negligence"

Defense Costs Reimbursable by Plaintiff in Frivolous Suits

Defense Costs Reimbursable by Plaintiff's Lawyer in Frivolous
Suits

Structured Settlements and Awards

Itemized Verdicts

Eliminate Joint and Several Liability

Change Collateral Source Rule

Insurance Companies

Prohibit Withdrawal from Geographic Areas

Require North Carolina Rating

Prohibit Disruptive Marketing Strategies

Midterm Cancellations

Cancellation of Agency Contracts

Market Assistance Program

Seek to Lengthen Term of Contract From One to Three Years With
Limitations on Annual Permitted Premium Increase

Seek Guaranteed Renewable Policies at Some Variable Rate

Provide Mandatory "Tail Coverage" in New Commercial General
Liability Policy Form

Prohibit Punitive Damages Being Paid by Insurance Companies
Statutes to Prevent Redlining

Nonlegislative Recommendations

Limit State and Federal Statutory Requirements for Liability
Insurance

Support Federal Redefinition of Joint and Several Liability
Encouraging Better Risk Management Practices
Educating the Public About the Costs of Lawsuits and Liability
Claims

Dram Shop

Cap on Dram Shop Liability Awards

Insurance Regulation

Insurance Pools Under Supervision of Insurance Department
Expand Power and Ability of Insurance Commissioner to Regulate
Premiums in Nonessential Lines of Insurance

Insurance Department Authorized to Require Participation in Joint
Underwriting Authority in Critically Underserved Areas

Expansion of FAIR and/or Beach Plan to Include:

Entire State

Other Lines Like Commercial General Liability

Expansion of Designated Agent Concept to Other Than Automobile
Insurance

Authorize Commissioner to Impose Six Month Moratorium on Agency
Cancellations

Statutory Requirement for Sixty Day Notification for
Cancellation of Policy
Non-Renewal of Policy
More Than One Hundred Percent Increase/Decrease in Premium

Statutory Definition of Unfair Trade Practices

Establish Minimum Activity Standards as Condition For Doing
Business in North Carolina:

Require Insurers to Actively Market in Eighty or More
Counties
Require Insurers to Offer At Least Seventy-Five Percent of
Their Product Lines in North Carolina

Place Non-Regulated Lines in Prior Approval Category

Statutory Authority for Banks and Brokerage Houses to Enter
Reinsurance Market

In Application for Certificate of Authority Require Assertion that
Company Will:

Use N.C. Data Experience in Setting Rates (Where Credible)
Not Sell Any Policy at Less than Ninety Percent of Actuarially
Sound Rate for Risk Assumed

Statutory Requirement for Department of Insurance Approval of
Acquisition of Domestic Insurers

Alternative Insurance Unit in Department of Insurance to Assist
Groups Looking to "Self Insure" or "Bulk Purchase"

Day Care Providers

Market Assistance Programs

Forming Joint Underwriting Associations

Establishing Assigned Risk Pools

Placing Limits on Verdicts Against Day Care Providers

Truckers

Establishing Assigned Risk Pool for Truckers

Placing Limits on Verdicts Against Truckers

Self Insurance by Trucker Organizations

Asbestos Abatement Contractors

Regulation of Asbestos Industry With Regard to:

Training

Licensing

Certification of Abatement Contractors

Placing a Statute of Limitations on the Time Within an Asbestosis

Lawsuit May Be Brought

The Commission considered the above list and after much debate and discussion narrowed the list to those issues the Commission felt could be successfully dealt with during the 1986 Session. The Commission Counsel was directed to prepare draft legislation covering the following items:

DRAFT LEGISLATION REQUESTS.

1. 60 Day Advance Notice on Non-Renewal or Premium Increases.
2. Anti-Redlining (Insurance Companies Must Meet Minimum Number of Markets).
3. Insurance Commissioner Authority to Provide Premium Tax Credits of Offsets to Companies Providing Insurance to Underserved Areas.
4. N.C. Loss Data Provided in Rate Filings/Using Credible N.C. Experience in Justifying Rate Increases.
5. Require Insurance Companies to Actuarily Justify Rate Increases.
6. Require Improved Data Reporting to Insurance Department.
7. Allow Higher Policy Limits in Facility Where Needed or Required by Statute or Regulation.

8. Cancellation of Agency Contracts.
9. Allow Banks to Enter Reinsurance Market.
10. Insurance Commissioner Authority to Supervise All Insurance Pools.
11. Third Party Claims Act/Fair Claims Act.
12. Insurance Commissioner Authority to Designate Agents in Underserved Territories.
13. Alternative Mechanism to Meet Financial Responsibility.
14. Limit or Caps on Noneconomic Damages (\$250,000).
15. Punitive Damages.
16. Modification of Joint and Several Liability.
17. Limit or Caps on Suits Against Local Governments.
18. Define Governmental Functions of Local Governments.
19. Collateral Source Rule Modification.
20. Structured Settlements and Awards.
21. Frivolous Suits, Dilatory Tactics, Product Liability Suits Against Retailers.

The Commission met in Raleigh on April 16, 1986 and considered several proposed drafts. After detailed discussion of the proposed legislation and the policy considerations included, the Commission directed the Counsel to further refine the legislation.

The Commission held a meeting in Raleigh on May 13, 1986 to hear comments from interested persons and organizations on the modified legislative proposals. The Commission decided to meet one additional time on May 27, 1986, the final work session before the 1986 Session, to vote on its recommendations to the General Assembly.

The Commission met in Raleigh on May 27, 1986 to review the draft of a single bill (See Appendix G) to be referred to the 1986 General Assembly. The Commission members made specific language changes to the bill and thoroughly discussed all provisions of the bill. The Commission members' questions were answered by the Commissioner of Insurance and the Commission Counsel. A motion was made to the effect that once the bill was corrected to reflect the changes made at the meeting, that it be recommended to the General Assembly during the 1986 session. That motion was passed with two dissenters.

The Commission issued a one page report to accompany the recommended bill (See Appendix H).

1986 GENERAL ASSEMBLY ACTION

The bill was technically modified and introduced as Senate Bill 868 by Senator Hardison on June 9, 1986.

Beginning on June 10, 1986, Senate Judiciary Committee I, chaired by Senator Henson Barnes began extensive consideration of SB 868. During the consideration, which took more than 50 hours, and included a public hearing on June 18, 1986, the Senate Judiciary Committee I reviewed the bill line by line and approved more than 40 amendments.

On June 10, 1986, HB 1511 was introduced by Representative Nesbitt. This bill contained the recommendations of the Insurance Regulation Study Committee with respect to changes in automobile insurance as recommended by that interim committee. (See their report for an analysis of the provisions of the bill as introduced.)

Prior to June 19, 1986, the House Insurance Committee incorporated the liability insurance regulation provisions of SB 868, as it had been modified up to that time by the Senate Judiciary Committee I, into HB 1511. HB 1511 did not, at that time contain any of the civil justice modification provisions contained in either SB 868 as introduced or as modified by Senate Judiciary Committee I. HB 1511 was passed by the House on June 20, 1986 and sent to the Senate. On June 24, 1986, HB 1511 was

received by the Senate and referred to the Senate Insurance Committee.

On June 9, 1986, Senator Joe Johnson introduced SB 873 which contained insurance law technical amendments which was referred to the Senate Insurance Committee. That bill was amended and passed by the Senate and sent to the House where it was referred to the House Insurance Committee on June 24, 1986, where it was considered and passed by that Committee and rereferred to the House Courts Committee on July 8, 1986. During the deliberations in the House Insurance Committee the original June 19, 1986 liability insurance provisions from SB 868 and the automobile insurance changes all without the further recommendations of the Insurance Commissioner were incorporated into SB 873.

On June 26, 1986, SB 868 containing the modified liability insurance regulation provisions and the modified civil justice modification provisions was withdrawn from the Senate calendar and rereferred to the Senate Insurance Committee.

So, on June 26, 1986, the Senate Insurance Committee had before it both HB 1511 and SB 868. That Committee chose to incorporate the modifications of the liability insurance regulation provisions requested by the Insurance Commissioner into HB 1511, to include portions of the civil justice modification provisions relating to frivolous lawsuits requested by Senator Hardison, a member of the Senate Insurance Committee, and not to consider SB 868 which was ultimately reported unfavorably.

On June 30, 1986, a Senate Insurance Committee Substitute for HB 1511 was reported favorably to the Senate where it was passed and sent to the House.

On July 1, 1986, the Senate Committee substitute for the House Committee substitute was received by the House and referred to the House Courts Committee for concurrence or non-concurrence. According to the rules of the House and the Senate the only action available to the House Committee was acceptance or rejection of the submitted committee substitute without further amendments.

On July 9, 1986, the House Committee incorporated modified provisions relating to frivolous lawsuits into SB 873 and failed to concur with the Senate Committee Substitute to HB 1511. The House passed the modified Senate Committee Substitute to SB 873 on July 11, 1986 and returned that bill for concurrence to the Senate. On July 11, 1986 the Senate failed to concur in the changes made in its committee substitute by the House.

On July 14, 1986 conference committees were appointed by the House and Senate on SB 873 and HB 1511.

On July 15, 1986 the House and Senate adopted the reports of the conferees on SB 873 and postponed HB 1511 indefinitely. SB 873 was ratified on July 16, 1986 as Chapter 1027 of the 1985 Session Laws (1986 Session).

Appendix I is a report by the Commission Counsel describing the contents of Chapter 1027 of the 1985 Session Laws.

FURTHER COMMISSION PROCEEDINGS

The Commission met in Raleigh on December 4, 1986 to review the actions of the 1986 Session of the General Assembly and to determine the future of the Commission's work. After hearing presentations from representatives of the North Carolina Society of Anesthesiology, the North Carolina County Commissioner's Association, the Department of Insurance, the North Carolina League of Municipalities, the Independent Insurance Agents and Professional Insurance Agents of North Carolina, the North Carolina Merchant's Association, the North Carolina Medical Society, the United Daycare Associates, the National Federation of Independent Businesses, the Commission decided to continue to meet and address the issues affecting the citizens of North Carolina with respect to the cost and availability of liability insurance. The Commission decided to focus in on the issues of the costs of the present system and whether or not the public could continue to pay for the current tort system through the higher and higher insurance premiums, joint and several liability, caps on various damages, punitive damages, and structured payments. The Commission directed the Commission Counsel to prepare a report on what other states were doing with respect to these issues.

The Commission met on January 7, 1987 in Raleigh to continue its consideration of the specific issues decided upon at the last meeting. The Commission hear from representatives of the Durham

Corporation, the North Carolina Citizens for Business and Industry, the North Carolina Bar Association, and the North Carolina Medical Society. The Commission Counsel distributed two reports, one from the Alliance of American Insurers and one prepared by himself (See Appendix J) detailing the actions taken and rejected by the various states during their latest legislative sessions on various tort reforms. The Commission decided to narrow the scope of the legislation that it would consider offering to the 1987 Session: punitive damages, political subdivision tort claims act, joint and several liability, caps on noneconomic loss, and collateral sources. The Commission directed the Commission Counsel to prepare legislation in these areas for consideration at the next meeting.

The Commission met on January 10, 1987 in Raleigh to review drafts prepared by the Commission Counsel in response to the instructions of the Commission from its last meeting. The Commission heard a report from Mr. John Beard, President of the North Carolina Bar Association who presented the findings of the Association's Special Committee on the Tort Liability System. (A copy of the report is attached to the full minutes of the meeting.) Mr. Paul Michaels of the Bar Association joined Mr. Beard in responding to questions from the Commission and from public members. Mr. Fred Baggett of the N.C. League of Municipalities discussed local governments and subrogation and the collateral source rule.

The Commission discussed the drafts prepared for the meeting, in detail, and made substantive changes to the language of the drafts and requested that they be redrafted for consideration at the next meeting.

The Commission met on January 30, 1987 in Raleigh and heard two presentations from Mr. David Blackwell representing the N.C. Academy of Trial Attorneys and Mr. Sammy Thompson representing the N.C. Association of Defense Attorneys. The Commission considered the drafts prepared for the meeting and approved six drafts for consideration by the 1987 General Assembly (See Appendix K). The Commission also considered several additions to this report and approved them and authorized the Commission CoChairmen and the Commission Counsel to prepare and submit the report to the General Assembly.

Note that detailed minutes and copies of all presentations made to the Commission at all of its meetings and to the legislative committees are on file and may be reviewed at the Legislative Library.

APPENDIX A

LIABILITY AND PROPERTY INSURANCE BILLS AND STATUTES CONSIDERED BY THE 1985 GENERAL ASSEMBLY

Liability and property insurance was the topic of 21 bills considered by the 1985 General Assembly. The following were considered:

[This index, prepared by the Institute of Government, lists twenty-one bills relating to liability and property insurance of which twelve or 57% were enacted into law.

**HB 344 (Ratified as Chapter 792) established this liability and Property Insurance Markets Study Committee.

**HB 456 (Ratified as Chapter 733) increased the educational requirements for the licensing of fire and casualty and of life insurance agents and required notices of agency contract terminations to be sent to the Commissioner stating the types and number of policies written through the agency being terminated.

**HB 700 (Ratified as Chapter 313) allows life insurance companies to invest their funds in obligations issued, assumed, or guaranteed by the African Development Bank.

**HB 763 was the original bill authorizing this study and was incorporated in the independent study bill ratified as Chapter 792.

**HB 1036 (Ratified as Chapter 489) clarified from which companies liability insurance may be purchased by Boards of Trustees in the Community College System.

**HB 1101 (Ratified as Chapter 770) provided for appointments to various boards and commissions by the Speaker of the House of Representatives.

**HB 1188 (Ratified as Chapter 679) prohibited certain financial institutions from requiring the purchase of insurance from the lender or an affiliate or subsidiary of the lender as a precondition for any action on a loan.

**SB 1 (Ratified as Chapter 479) provided for Department of Insurance current budget operations for the.

**SB 636 (Ratified as Chapter 790) provided the statutory authority for the Legislative Research Commission to study Medical Malpractice and Liability as proposed by SB 703 introduced by Senator Taft.

**SB 703 (Ratified as Chapter 790) provided for a study of Medical Malpractice and Liability.

**SB 738 (Ratified as Chapter 666) made technical and other needed changes to improve the regulation of insurance.

**SB 742 (Ratified as Chapter 527) clarified the risks against which a local school board could purchase insurance and the companies that could sell than insurance.

APPENDIX B

BASIC CONCEPTS

Certain basic concepts should be familiar to the reader of this report in order to comprehend the nature of the discussions and debate over the marketing of property and liability insurance.

The following lists of concepts is included to assist in preparing the reader to understand what follows:

The contract of insurance, made between parties usually called the insured and the insurer, is distinguished by the presence of five elements:

- (a) The insured possesses an interest of some kind susceptible of pecuniary estimation, known as an insurable interest.
- (b) The insured is subject to a risk of loss through the destruction or impairment of that interest by the happening of designated perils.
- (c) The insurer assumes that risk of loss.
- (d) Such assumption is part of a general scheme to distribute actual losses among a large group of persons bearing somewhat similar risks.
- (e) As consideration for the insurer's promise, the insured makes a ratable contribution, called a premium, to a general insurance fund.

A contract possessing only the three elements first named is a risk-shifting device, but not a contract of insurance, which is a risk-distributing device; but, if it possesses the other two as well, it is a contract of insurance, whatever be its name or its form.¹

I. THE LIABILITY RISK

The scope and magnitude of the liability risk involve every modern family or organization with increasing legal responsibility. The legal basis for liability is legal wrongs, invading the rights of others. Legal wrongs may be criminal or civil. Criminal wrongs involve the public at large and are punishable by government action. Civil (or private) wrongs are based on (1) contracts or (2) torts.

Liability under contract law occurs only as a result of the invasion of another's rights under a contract by:

Breach of contract, or not fulfilling promises in an agreement;

Bailee liability, or not fulfilling the duty of care by a person who has intentionally received temporary custody of goods or property of others;

¹Excerpt from Vance on Insurance, Third Edition, West Publishing Co., 1951.

Implied warranties, which often extend liability well beyond the specific written obligations of a contract. Liability under tort law involves all civil wrongs not based on contracts:

Intentional acts or omissions, such as battery, assault, and trespass;

Strict or absolute liability, which applies even if there is no fault present; and

Negligence liability, which requires:

A legal duty to act or not act, under the circumstances;

A voluntary unintentional wrong, as determined by as prudent person's conduct;

A proximate relationship between the wrong, and

An injury, a death, or property damage as a result.

Modifications of the usual negligence liability rules sometimes occur by court cases or statutes:

Comparative negligence, where each party causing losses pays in the proportion that he or she is liable;

Presumed negligence, which under certain circumstances may create a "prima facie" case of liability; and

Imputed negligence, which may extend the liability of some persons or organizations (such as employers, parents, automobile owners, and others) to injuries or damages caused by others.

Specific kinds of liability situations illustrate wide variety based upon: real property ownership, attractive nuisance hazards, (injuries to children), employees and agents, animals, government units and charitable institutions, nonownership liability (automobiles), and libel and other related types of liability.

II. GENERAL LIABILITY INSURANCE

Liability risk management coordinates other methods with insurance.

Types of liability insurance losses are classified into major types as bodily injury and property damage; and direct and contingent.

The scope of major liability insurance contracts includes (1) employers, (2) automobile, and (3) "general" which is further subdivided into: (1) personal, (2) business, and (3) professional contracts; or (1) primary and (2) excess contracts; and medical payments.

The general liability insurance program is discussed:

Nature of and rationale for the revisions.

The basic policy format, with the three following parts:

Declarations, including statements by the insured about the coverage,

The policy jacket, with supplementary payments, definitions, and conditions applying to all general liability contracts of this type, and

The coverage parts, which contain the insuring agreements and exclusions.

Personal liability insurance contracts, the comprehensive personal liability policy and farmers' CPL, cover individual and family interests.

Business liability insurance contracts are numerous. Most common are:

Owners', landlords', and tenants' liability policy (OLT).

Manufacturers' and contractors' liability policy (M&C).

Comprehensive general liability policy (CGL).

Other business liability coverages: storekeepers', contractual, products and completed operations, protective, and automobile.

Professional or malpractice liability insurance contracts differ greatly and are important to medical and many other professional persons.

Excess insurance is broad, high-limit coverage of catastrophic losses of individuals and businesses. This is contrasted with "primary" coverages which pay losses first (or are the only protection), before the excess contracts apply:

Excess and surplus lines, often insuring risks difficult to place in normal markets,

Differences in conditions coverage, for all-risks physical damage and worldwide protection.

The umbrella liability policy, a popular form for businesses needing broader, higher limit insurance, and

Excess personal liability policies, for million-dollar or higher limit personal coverages.

Medical payments coverage pays medical expenses, regardless of liability, and is often included in general liability contracts.

III. PROPERTY AND LIABILITY INSURANCE

Miscellaneous property and liability insurance is a broad field:

Aviation insurance has developed rapidly in the "jet age."

Insurers include several large syndicates, or groups of insurers.

Basic nature is like that of auto insurance, but with larger exposures.

Aircraft classification: airline, private, industrial, commercial, special.

Types of contracts include hull, aircraft liability, admitted liability, medical payments, and comprehensive light plane.

Aviation rates are nonstandard, open market, and international.

Boiler and machinery insurance combines property-liability insurance:

Nature: direct and indirect losses to insured's property. Liability to others for their property or injury losses is included as direct loss.

The basic contract is written separately, or with special multiperil policies.

Direct losses are those by explosion, collapse, rupture, and other breakdowns of steam boilers, machinery, or electrical equipment.

Indirect losses include consequential, use and occupancy, outage, and power interruption.

Glass insurance is for expensive plate glass and other special types.

Basic coverages are for "all risks" of breakage or damage by chemicals with fast replacement of glass an important service.

Credit insurance is catastrophe protection, for wholesalers primarily.

Nature and development, a guarantee with insurance characteristics.

Foreign or export credit insurance, helping to expand world trade.

Underwriting the risk, based on credit ratings and coinsurance.

The peril covered: insolvency of, or uncollectibility from, customers.

Types of contract include general and extraordinary.

Policy provisions define insolvency, normal loss, and other terms.

Title insurance is important only in some geographic areas: The peril insured is undiscovered past defects in real estate title.

The need arises from human errors in meeting legal requirements.

The title insurer has extensive abstract research facilities.

The basic policy is for indemnity to owners or mortgagees.

Contract provisions include claim conditions and term (perpetual).

Use of group policy by mortgage companies is convenient.

IV. MULTIPLE-LINE AND ALL-LINES INSURANCE

Multiple-line and all-lines insurance trends in the U.S. are very important.

Product diversification trends "spread the risk" among various major lines of insurance; expansion to related financial services is emerging.

Multiple-line insurance characteristics include its--

Nature, a combination of traditional fire and casualty insurance.

Development, which has been strong since the multiple-line laws.

Significance, approximately \$12 billion annual sales and many changes.

Purposes, which are summarized in its--

Policyholder advantages of coverage, cost, and convenience.

Insurer advantages of the same type, plus greater stability.

Disadvantages, restricting flexibility and causing misunderstanding.

Multiple-lines insurance contracts are different from multiple-lines insurers or groups; or from multiple-peril, package, or all-risks contracts.

Personal multiple-line contracts have been very popular.

Homeowners' policies analysis centers on--who (persons), what (property and perils), when (policy duration), where (places), and how coverage applies (package, perils, premiums, etc.).

Mobilehome policy is similar to the homeowners' contract.

Farmowner-ranchowner's policy combines business and personal exposures.

Other personal multiple-line contracts for valuable articles.

Business multiple-line insurance contracts have grown rapidly since the early manufacturer's and block policies, particularly with the popular:

Special multiperil (SMP) policies now available to almost all commercial risks, combining broad coverage for property-liability perils.

Businessowners' policies (BOP), in the new "readable" type package contract for smaller apartment, office, and retail store businesses.

All-lines insurance is a separate and more recent trend.

Nature and extent: writing fire, casualty, life, and health perils.

Property-liability insurers have often become all-lines groups by forming or purchasing life insurer affiliates, or through holding companies.

The future promises greater acceptance of this idea, including all-lines contracts insuring home, auto, life, and health perils in one combination personal-lines package policy.

Financial services conglomerates are also a significant trend to watch.

Mergers and growth of business take several forms.

The position of insurance in these changes is controversial, but increasing.

APPENDIX C
AUTHORIZING LEGISLATION

CHAPTER 792
HOUSE BILL 344

AN ACT TO CREATE AND CONTINUE VARIOUS COMMITTEES AND COMMISSIONS,
TO MAKE APPROPRIATIONS THEREFOR, AND TO AMEND STATUTORY LAW.

The General Assembly of North Carolina enacts:

Section 1. This act shall be known as "The Independent Study Commissions and Committees Act of 1985."

An outline of the provisions of the act follows this section. The outline shows the heading "-----CONTENTS/INDEX-----" and lists by general category the descriptive captions for the various sections and groups of sections that compile the act.

-----CONTENTS/INDEX-----

This outline is designed for reference only, and the outline and the corresponding entries throughout the act in no way limit, define, or prescribe the scope or application of the text of the act. The listing of the original bill or resolution in the outline of this act is for reference purposes only and shall not be deemed to have incorporated by reference any of the provisions contained in the original bill or resolution.

* * * * *

PART VII.-----LIABILITY AND PROPERTY INSURANCE MARKETS STUDY COMMISSION

(H. B. 763 - Hasty).

Sec. 8.1
Sec. 8.2
Sec. 8.3
Sec. 8.4
Sec. 8.5

PART XX. -----EFFECTIVE DATE

Sec. 21

* * * * *

PART VII.-----LIABILITY AND PROPERTY INSURANCE MARKETS STUDY COMMISSION.

Sec. 8.1. There is created the Commission to examine Liability and Property Insurance Markets, hereinafter referred to as "the Commission". The Commission shall consist of 12 members, appointed as follows:

(a) The Speaker of the House shall appoint four members: three of whom shall be members of the House of Representatives; and one of whom shall be a fire and casualty insurance agent duly licensed by this State, who may also be a member of the North Carolina House of Representatives.

(b) The President of the Senate shall appoint four members: three of whom shall be members of the North Carolina Senate; and one of whom shall be a representative of a fire and casualty insurer duly licensed to transact the business of

insurance in this State, who may also be a member of the North Carolina Senate.

(c) The Commissioner of Insurance shall appoint four members: two of whom shall be members of the general public; one of whom shall be a fire and casualty insurance agent duly licensed by the State; and one of whom shall be a representative of a fire and casualty insurer duly licensed to transact the business of insurance in this State.

In the event of a vacancy, the appropriate appointing authority shall appoint a replacement to serve the remainder of the unexpired term. Legislative members of the Commission shall be paid subsistence and mileage allowances authorized by G.S. 120-3.1 for services on the Commission when the General Assembly is not in session. Other members of the Commission shall be paid the per diem and allowances authorized by G.S. 138-5. The Speaker of the House of Representatives and the President of the Senate shall each appoint from their appointees one member from the House of Representatives and from the Senate who will serve as cochairs of the Commission.

Sec. 8.2. The Commission is authorized to review, analyze, and report on:

(a) The availability of professional and commercial liability and property insurance in this State and the factors causing and compounding diminutions in underwriting capacity.

(b) The underwriting and marketing practices of admitted and nonadmitted liability and property insurers and producers doing business in this State.

(c) Optional methods of risk management and risk sharing that may be utilized by the citizens of this State.

(d) The effect of diminished underwriting capacity in professional and commercial liability and property insurance on the economy of this State.

(e) Any other subjects deemed by the Commission to be relevant to this study.

Sec. 8.3. With the prior approval of the Legislative Services Commission, the Commission may meet in the State Legislative Building or Legislative Office Building and utilize the services of the clerical and professional staff of the Legislative Services Office. The Commission may utilize the staff of the Department of Insurance.

Sec. 8.4. The Commission shall submit a final report to the 1987 General Assembly on its convening date.

Sec. 8.5. There is appropriated from the General Fund to the Legislative Services Commission for fiscal year 1985-86 the sum of seventeen thousand dollars (\$17,000) to carry out the provisions of this Part.

* * * * *

PART XX.----EFFECTIVE DATE.

Sec. 21. This act is effective upon ratification.

In the General Assembly read three times and ratified, this 18th day of July, 1985.

Robert B. Jordan III
President of the Senate

Liston B. Ramsey
Speaker of the House of
Representatives

APPENDIX D

LIABILITY AND PROPERTY INSURANCE MARKETS COMMISSION MEMBERSHIP

Rep. John C. "Pete" Hasty (Cochairman) 1181 W. Sanders Street Maxton, N.C. 28364	Senator Harold W. Hardison (Cochairman) 1001 W. Vernon Avenue Kinston, N.C. 28501
Joseph A. Bambury, Jr. Royal Insurance P.O. Box 2488 Charlotte, N.C. 28211	Senator Joe Johnson P.O. Box 750 Raleigh, N.C. 27602
Rep. R. D. Beard 2918 Skye Drive Fayetteville, N.C. 28303	Rep. John B. McLaughlin Box 158 Newell, N.C. 28126
Mr. Dale Bennett Harleysville Mutual Ins. Co. P.O. Box 22300 Greensboro, N.C. 27420	Rep. Wendell H. Murphy P.O. Box 759 Rose Hill, N.C. 28458
Mr. Harry W. Clarke President Western Carolina Industries, Inc. 542 Hendersonville Street Asheville, N.C. 28803	H. Glenn Powell Glenn Powell Agency P.O. 18567 Raleigh, N.C. 27609
Senator James C. Johnson, Jr. 29 Church Street, SE Concord, N.C. 28025	C. J. Spivey Ins. and Risk Mgt. Committee of Mecklenburg County 301 S. McDowell Street Suite 1008 Charlotte, N.C. 28204-2677
Kenneth T. Levenbook, Counsel	
Julia H. Braswell, Clerk	

APPENDIX E

PERSONS MAKING PRESENTATIONS TO THE COMMISSION

October 22, 1986 (Raleigh)

Commissioner James E. Long
Glenn Douden, Nationwide Insurance
Jay Johnson, Reinsurance Intermediaries
Merritt Jones, Independent Insurance Agents of North Carolina
Paul Hoover, Carolina Association of Professional Insurance Agents
Ron Aycock, N.C. Association of County Commissioners
Fred Baggett, Counsel to the N.C. League of Municipalities
J. Wilson Hunt, Public Officers and Employees Liability Comm.
Paul Lawler, Citizens for Business and Industry
Durwood Laughinghouse, Professional Engineers of N.C.
Ron Anderson, Professional Engineers of N.C.
T. Jerry Williams, N.C. Restaurant Association
Eugene Hafer, N.C. Hotel and Motel Association
Emmett Patterson, N.C. Association of Electric Cooperatives
Carl Staley, United Daycare Services
Anne Allen, Department of Human Resources
J. Ruffin Bailey, American Insurance Assocation

November 13, 1985 (Kinston)

Donald B. Boldt, Wall Lenk Corporation
E. Walker Sugg, Edwards Group of businesses
Gilbert R. Alligood, P.E., Rivers and Associates, Inc.
Charles Proffitt, P.E., Fenner and Proffitt, Inc.
Larry P. Meadows, Jones County Administrator
Don McGlohon, independent insurance agent
Carl Pate, small business operator from Beulahville, N.C.
Cloyce Anders, independent insurance agent
Jerry E. Cox, Assistant City Manager, City of Greenville
Marty Beam, W.A. Moore & Company
Rick Holder, L. Harvey & Son Co., Tidewater Transit Company
Gene Leggett, Professional Marine Surveyors
Ralph Cottle, Duplin County

November 14, 1986 (Laurinburg)

Sam Snowdon, AIA, Snowdon, Stogner & Associates
Edgar Roberts, Mayor of Pinehurst
David Walker, independent insurance agent
Lacy H. Koonce, Jr., P.E., Noble & Associates, Inc.
Judy W. Clemonns, Brunswick Insurance Services, Inc.
Terry R. Garner, Maxton Town Attorney
Wade Dunbar, Dunbar Insurance Agency
Reg Poteat, Poteat Insurance Agency
T. Y. Hester, Jr., Robeson County Personnel Director
Gaines Grantham, Grantham Insurance

December 4, 1985 (Asheville)

Hugh Morton, President, Grandfather Mountain
David A. Flippin, Municipal Risk Manager
John M. Sharbaugh, N.C. Association of CPA's
Jeff Reece, Jr., P.E., Reece, Noland, & McElrath
Steve Scarborough, Autrey-Smathers Insurance Agency
Kirby Grant Ensley
Kenneth Cosgrove, M.D., President, N.C. Medical Society
Bruce Elmore, J.D.
Betty L. Buss, Buss Automation, Inc.
John Henderson, M.D., surgeon
Jim Neal

December 5, 1985 (Charlotte)

Dwight Gay, American Insurance Consultants
Harold F. McKnight, P.E.
George McCarthy, Risk Manager for City of Fayetteville
Jim Long, Commissioner of Insurance
Ralph Broome, independent insurance agent
Robert Cooper, Cooper Petroleum, Inc.
Jim Richie, North Carolina Public Transportation Association
Frank Watson, Charlotte Van & Storage Company
Eddie Knox, J.D.
Charles Beard, Risk Manager of Wake County
Richard Heckle, Dean, Heckle & Hill, Inc.
Carl Hurley, Jr., nurse midwife
Emily Ousley, nurse midwife
Emily Turner, Turner Oil Company
Jane Chance, Carolina Motor Club
Doug House, Duke Power Company Risk Manager
Robert C. Dellinginger, A.I.A.
Ralph Whitehead, P.E.
T. S. Jones, Anson County Manager
Pam Fisher, Coe Insurance Agency

Larry Matthews (by written submission)

February 3, 1986 (Raleigh)

J. Michael Crowell, N.C. Association of Convenience Stores
T. Jerry Williams, N.C. Restaurant Association
Rick Coker, Cataloochee Ski Center
Rodney B. Graham, Jr., Wade Manufacturing Company
Harvey B. Mathias, N.C. League of Municipalities
James Blackburn, III, N.C. Association of County Commissioners
Durwood Laughinghouse, Professional Engineers of N.C.
Jim Maxwell, N.C. Academy of Trial Attorneys
John W. Morris, N.C. Bar Association
George E. Moore, N.C. Medical Society
Thomas S. Carpenter, Aetna Life & Casualty Insurance, Co.
J. Ruffin Bailey, American Insurance Association
George Teague, Alliance of American Insurers
Phil Godwin, National Association of Independent Insurers
Jim Long, Commissioner of Insurance

April 1, 1986 (Raleigh)
COMMISSION WORK SESSION

April 16, 1986 (Raleigh)
COMMISSION WORK SESSION

May 13, 1986 (Raleigh)

Lacy H. Thornburg, Attorney General
James C. Fuller, Jr., N.C. Academy of Trial Attorneys
Grover C. McCain, Jr., N.C. Bar Association
Irving Joyner, N.C. Black Lawyer's Association
John T. Henley, N.C. Project, Inc.
Jim Blackburn, N.C. Association of County Commissioners
Neil Ellis, N.C. Project, Inc.
J. Ruffin Bailey, American Insurance Association
Jim Long, Commissioner of Insurance
Edith Marsh

May 27, 1986 (Raleigh)
Jim Long, Commissioner of Insurance
B.F. Seagle, III, Aetna Life & Casualty

December 4, 1986 (Raleigh)

Dr. H. Ryland Vest, North Carolina Society of Anesthesiology
Ron Aycock, North Carolina County Commissioner's Association
Jim Long, Insurance Commissioner
Harvey Mathias, North Carolina League of Municipalities
John Bode, Independent Insurance Agents and Professional Insurance Agents of North Carolina
Bill Rustin, North Carolina Merchant's Association
Glen Jenigan, North Carolina Medical Society
Carl Staley, United Daycare Associates
Susan Valuri, National Federation of Independent Businesses

January 7, 1987 (Raleigh)

William M. Trott, Attorney
John Bergin, North Carolina Citizens for Business and Industry
John Morris, North Carolina Bar Association
Glen Jernigan, North Carolina Medical Society
Ruffin Bailey, American Insurance Association
William Hale, Department of Insurance

January 10, 1987 (Raleigh)

John Beard, President, North Carolina Bar Association
Paul Michaels, North Carolina Bar Association
Fred Baggett, North Carolina League of Municipalities

January 30, 1987 (Raleigh)

David Blackwell, Executive Vice-President, N.C. Academy of Trial Attorneys
Sammy Thompson, N.C. Association of Defense Attorneys

APPENDIX F

MAILING LIST

Conrad Airall Legislative Research Div.	John R. Andrew Andrew and Kuske Consulting Engineers
Ron Aycock N.C. Association of County Commissioners	Roy L. Baber, Jr. Professional Engineers of North Carolina
Fred Baggett N.C. League of Municipalities	J. Ruffin Bailey American Insurance Association
Jim Blackburn N.C. Association of County Commissioners	Jan Ramquist N.C. Academy of Trial Attorneys
J. Melville Broughton, Jr.	Charles Case
J. Michael Crowell Tharrington, Smith & Hargrove	Glenn Douden Regional Commerical Manager Nationwide Insurance
Elizabeth Drury DHR Office of Legislative & Legal Affairs	Joseph W. Eason
Charles E. Gordon Building Division Manager Assoc. of General Contractors	Eugene Hafer
Bill Hale Legal Division Department of Insurance	Mic Harris Carolina Carriers, Inc.
Glascow Hicks, Jr. Hanover Excess & Surplus	Bill Holman
Robert P. Hopkins Consulting Engineering Council	J. Wilson Hunt The Hunt Agency
David King N.C. Dept. of Transportation	Joe R. Kluttz, Jr. Albemarle Insurance Agency

Durwood Laughinghouse Professional Engineers of N.C.	Paul Lawler NC Citizens for Business and Industry
Jovita Mask CAPIA	Harvey Mathias Director of Insurance Services N.C. League of Municipalities
John B. McMillan Manning, Fulton & Skinner	William Patterson
Bill Rustin N.C. Retail Merchants	Terri Saylor Olson Management Group
B.F. Seagle, III Aetna Life & Casualty	Patrick B. Simmons N.C. Dept. of Transportation
J. Dal Snipes Snipes Ins. Service, Inc.	Craig Souza NC Health Care Facilities Assn.
Carl Staley United Daycare Services	Tommy Sutton J.T. Sutton Ins. Agency, Inc.
William M. Trott Young, Moore, Henderson & Alvis, P.A.	Susan R. Valuri State Dir., National Fed. of Independent Business
Fletcher Willye Kellogg-Morgan Association	Jack Betts Associate Editor North Carolina Insight
Jane Sharp N.C.C.C.	Ken Brady Reporter - WITN-TV
Steve Morisette N.C. Hospital Association	Lela Phillips Town of Murphy
Jim Ritchey Winston-Salem Transit Authy.	George M. Teague Alliance of American Insurers
Phil Godwin Nat'l Assn. of Indpendent Insurers	Todd Cohen Business Editor News & Observer

John Langley, M.D.	Jack Stevens
James E. Long Commissioner of Insurance	Phil Sallings U.S.F. & G.
George Moore N.C. Medical Society	T. Jerry Williams N.C. Restaurant Association
E. Ann Christian Legislative Counsel N.C. Bar Association	Catherine D. Ferrell Government Relations Manager The Convenience Store Group
Linda Little Governor's Waste Mgt. Board	David Willett
Scott C. Gayle Fisher, Fisher & Gayle	Miriam Block N.C. Assn. of Girl Scout Councils
Millie Buchanan Project FireHAT	Sam Johnson
R. Michael Jones C.P. & L.	Sue Robertson
Ellyn Silverman, M.P.H. American Diabetes Assn., N.C. Affiliate	Alan Briggs Deputy Attorney General
Jim Gulick Special Deputy Attorney General	John Ingram
Charles H. Mercer, Jr.	Karen Murphy McCain & Essen
Suzy Thompson Southern Strategies	

APPENDIX G

PROPOSED LEGISLATION--CONSOLIDATED

A BILL TO BE ENTITLED
AN ACT TO IMPLEMENT THE RECOMMENDATIONS OF THE LIABILITY AND
PROPERTY INSURANCE MARKETS STUDY COMMISSION.

The General Assembly of North Carolina enacts:

Section 1. General Statute Chapter 58 is amended by adding a new Article 38 to read:

"Article 38

"Insurance Regulatory Reform Act.

"<58-470. Short title.--This Article shall be known and may be cited as the Insurance Regulatory Reform Act.

"<58-471. Legislative findings and intent.--(a) Due to conditions in national and international property and liability insurance markets, insureds in the United States have experienced unprecedented in-term cancellations of existing policies for entire books of business, have been afforded little or no notice that existing policies would not be renewed at their expiration dates or would be renewed only at substantially higher rates or on less favorable terms. The General Assembly finds that such conditions pose an imminent peril to the public welfare for the following reasons:

- (1) In-term cancellations of insurance coverages erode insureds' confidence and breach insureds' trust; unfairly and prematurely terminate the promised coverage; force persons to go without needed insurance protection or force the procurement of substitute insurance at greater cost; and create marketplace confusion resulting in product unavailability.
- (2) Failures to provide timely notices of nonrenewals or of renewals with altered terms deprive persons of adequate opportunities to secure affordable replacement coverages or require persons to go without needed insurance protection.

(b) The General Assembly finds that there is no uniform requirement for the notice of cancellation, renewal or nonrenewal for commercial property and liability insurance and that it should adopt reasonable requirements for such notices and should regulate in-term cancellations of entire books of business by companies.

"<58-472. Scope.--(a) Except as otherwise provided, this Article applies to all kinds of insurance authorized by G.S. 58-72(4) through (14) and G.S. 58-72(18) through (22), and to all insurance companies licensed by the Commissioner to write those kinds of insurance. This Article does not apply to kinds of

insurance written under Articles 12B, 18A, 18B, 25A or 36 of this Chapter; to marine and personal inland marine insurance; to aviation insurance; nor to policies issued in this State covering risks with multistate locations, except with respect to coverages applicable to locations within this State.

(b) This Article is not exclusive, and the Commissioner may also consider other provisions of this Chapter to be applicable to the circumstances or situations addressed in this Article. Policies may provide terms more favorable to insureds than are required by this Article. The rights provided by this Article are in addition to and do not prejudice any other rights the insured may have at common law, under statutes, or under administrative rules.

"<58-473. Certain policy cancellations prohibited.--(a) No insurance policy or renewal thereof may be cancelled by the insurer prior to the expiration of the term stated in the policy and without the prior written consent of the insured, except for any one of the following reasons:

- (1) Nonpayment of premium in accordance with the policy terms;
- (2) An act or omission by the insured or his representative that constitutes material misrepresentation or nondisclosure of a material fact in obtaining the policy, continuing the policy, or presenting a claim under the policy;
- (3) Increased hazard or material change in the risk assumed that could not have been reasonably contemplated by the parties at the time of assumption of the risk;
- (4) Substantial breach of contractual duties, conditions, or warranties that materially affects the insurability of the risk;
- (5) A fraudulent act against the company by the insured or his representative that materially affects the insurability of the risk;
- (6) Lack of cooperation from the insured or his representative on loss control matters that materially affect the insurability of the risk;
- (7) Loss of facultative reinsurance, or loss of or substantial changes in applicable reinsurance as provided in G.S. 58-475;
- (8) Conviction of the insured of a crime arising out of acts that materially affects the insurability of the risk; or
- (9) A determination by the Commissioner that the continuation of the policy would place the insurer in violation of the laws of this State.

(b) Any cancellation permitted by subsection (a) of this section is not effective unless written notice of cancellation has been delivered or mailed to the insured, not less than 15 days before the proposed effective date of cancellation. The notice

must be given or mailed to the insured, and any designated mortgagee or loss payee at their addresses shown in the policy or, if not indicated in the policy, at their last known addresses. The notice must state the precise reason for cancellation. Proof of mailing is sufficient proof of notice. Failure to send this notice to any designated mortgagee or loss payee invalidates the cancellation only as to the mortgagee's or loss payee's interest.

(c) This section does not apply to any insurance policy that has been in effect for less than 60 days and is not a renewal of a policy. That policy may be cancelled for any reason by furnishing to the insured at least 15 days prior written notice of and reasons for cancellation.

(d) Cancellation for nonpayment of premium is not effective if the amount due is paid before the effective date set forth in the notice of cancellation.

(e) Copies of the notice required by this section shall also be sent to the agent or broker of record; however, failure to send copies of the notice to such persons shall not invalidate the cancellation.

"<58-474. Notice of nonrenewal, premium increase, or change in coverage required.--(a) No insurer may refuse to renew an insurance policy except in accordance with the provisions of this section, and any nonrenewal attempted or made that is not in compliance with this section is not effective. This section does not apply if the policy holder has insured elsewhere, has accepted replacement coverage, or has requested or agreed to nonrenewal.

(b) An insurer may refuse to renew a policy that has been written for a term of one year or less at the policy's expiration date by giving or mailing written notice of nonrenewal to the insured not less than 45 days prior to the expiration date of the policy.

(c) An insurer may refuse to renew a policy that has been written for a term of more than one year or for an indefinite term at the policy anniversary date by giving or mailing written notice of nonrenewal to the insured not less than 45 days prior to the anniversary date of the policy.

(d) The notice required by this section must be given to the insured and any designated mortgagee or loss payee at their addresses shown in the policy or, if not indicated in the policy, at their last known addresses. Proof of mailing is sufficient proof of notice. The notice of nonrenewal must state the precise reason for nonrenewal. Failure to send this notice to any designated mortgagee or loss payee invalidates the nonrenewal only as to the mortgagee's or loss payee's interest.

(e) Copies of the notice required by this section shall also be sent to the agent or broker of record; however, failure to send copies of the notice to such persons shall not invalidate the nonrenewal.

"<58-475. Notice of renewal of policies with premium or coverage changes.--(a) If an insurer intends to renew a policy, the insurer must furnish to the insured the renewal terms and a

statement of the amount of premium due for the renewal policy period.

(b) If the policy being renewed was written for a term of one year or less, the renewal terms and statement of premium due must be given or mailed not less than 45 days before the expiration date of that policy. If the policy being renewed was written for a term of more than one year or for an indefinite term, the renewal terms and statement of premium due must be given or mailed not less than 45 days before the anniversary date of that policy. The renewal terms and statement of premium due must be given or mailed to the insured at their addresses shown in the policy, at their last known addresses.

(c) If the insurer fails to furnish the renewal terms and statement of premium due in the manner required by this section, the insured may cancel the renewal policy within the 30-day period following receipt of the renewal terms and statement of premium due. For refund purposes, earned premium for any period of coverage shall be calculated pro rata upon the premium applicable to the policy being renewed instead of the renewal policy.

(d) If a policy has been issued for a term longer than one year, and for additional consideration a premium has been guaranteed for the entire term, it is unlawful for the insurer to increase that premium or require policy deductibles or other policy or coverage provisions less favorable to the insure during the term of the policy.

(e) Copies of the notice required by this section shall also be given to any designated mortgagee or loss payee and may also be given to the agent or broker of record.

"<58-476. Reinsurance.--An insurer may cancel or refuse to renew a kind of insurance when the cancellation or nonrenewal is necessary because of a loss of or substantial reduction in applicable reinsurance, by filing a plan with the Commissioner pursuant to the requirements of this section. The insurer's plan must be filed with the Commissioner at least 10 days prior to the issuance of any notice of cancellation or nonrenewal. The insurer may implement its plan upon the approval of the Commissioner, which shall be granted or denied in writing, with reasons therefor, within 10 days of the Commissioner's receipt of the plan. Any plan submitted for approval shall contain a certification by an elected officer of the company:

- (1) that the loss or substantial change in applicable reinsurance necessitates the cancellation or nonrenewal action;
- (2) that the insurer has made a good faith effort to obtain replacement reinsurance but was unable to do so because of the unavailability or unaffordability of replacement reinsurance;
- (3) identifying the category of risks, the total number of risks written by the company in that category, and the number of risks intended to be cancelled or not renewed;

- (4) identifying the total amount of the insurer's net retention for the risks intended to be cancelled or not renewed;
- (5) identifying the total amount of risk ceded to each reinsurer and the portion of that total that is no longer available;
- (6) explaining how the loss of or reduction in reinsurance affects the insurer's risks throughout the kind of insurance proposed for cancellation or nonrenewal;
- (7) explaining why cancellation or nonrenewal is necessary to cure the loss of or reduction in reinsurance; and
- (8) explaining how the cancellations or nonrenewals, if approved, will be implemented and the steps that will be taken to ensure that the cancellation or nonrenewal decisions will not be applied in an arbitrary, capricious, or unfairly discriminatory manner.

"<58-477. Notice of cessation of business through insurance agency.--(a) Each insurer must, upon the cessation of any of its business through a North Carolina insurance agency, furnish the Commissioner with the following information on a form to be prescribed by the Commissioner:

- (1) The kinds of policies no longer written through the agency. In describing the kinds of these policies, those appearing on page 14 of the annual statement convention blank will suffice, except that liability coverages should be more specifically described;
- (2) The number of policies, by kind, no longer written through the agency;
- (3) A statement as to whether or not the cessation of business is by nonrenewal of business at policy expiration dates, or is a decision not to accept new business from the agency, or a combination of these;
- (4) If the cessation is made by the insurer, the specific reason or reasons for the cessation; and
- (5) The names and addresses of the insurer and the agency and the effective date of the cessation of the business.

(b) This section applies to the cessation of the writing of any kind of insurance subject to this Article through an agency located in North Carolina. Reports are required even though other kinds of insurance may still be written through the agency."

"<58-478. No liability for statements or communications made in good faith; prior notice to agents or brokers.--(a) There is no liability on the part of and no cause of action of any nature arises against any insurer or its authorized representatives, agents, or employees, or any licensed insurance agent or broker,

for any communication or statement made, unless shown to have been made in bad faith with malice, in any of the following:

- (1) A written notice of cancellation under G.S. 58-473, of nonrenewal under G.S. 58-474, or of cessation of business through an agency under G.S. 58-476, specifying the reasons therefor;
- (2) Communications providing information pertaining to such cancellation, nonrenewal, or cessation of business through an agency;
- (3) Evidence submitted at any court proceeding, administrative hearing, or informal inquiry in which such cancellation, nonrenewal, or cessation of business through an agency is an issue.

(b) With respect to the notices that must be given or mailed to agents or brokers under G.S. 58-473 and G.S. 58-474, the insurer may give or mail that notice at the same time or prior to giving or mailing the notice to the insured.

"<58-479. Termination of writing kind of insurance.--(a)

Except as provided in G.S. 58-475, no insurer may terminate, by nonrenewals, an entire book of business of any kind of insurance without 60 days prior written notice to the Commissioner; unless the Commissioner determines that continuation of the line of business would impair the solvency of the insurer or unless the Commissioner determines that such termination is effected under a plan that minimizes disruption in the marketplace or that makes provisions for alternative coverage at comparable rates and terms.

(b) Except as provided in G.S. 58-475, in-term cancellation by an insurer of an entire book of business of any kind of insurance is presumed to be unfair, inequitable, and contrary to the public interest, unless the Commissioner determines that continuation of the line of business would impair the solvency of the insurer or unless the Commissioner determines that such termination is effected under a plan that minimizes disruption in the marketplace or that makes provisions for alternative coverage at comparable rates and terms.

"<58-480. Policy form and rate filings; punitive damages; data required to support filings.--(a) With the exception of inland marine insurance, which by general custom of the business is not written according to manual rates and rating plans, all policy forms must be filed with and either approved by the Commissioner or 90 days have elapsed and he has not disapproved the form before they may be used in this State. With respect to liability insurance policy forms, an insurer may exclude or limit coverage for punitive damages awarded against its insured.

(b) With the exception of inland marine insurance, which by general custom of the business is not written according to manual rates and rating plans, all rates by licensed fire and casualty companies or their designated rating organizations must be filed with the Commissioner at least 60 days before they may be used in this State.

(c) A filing that does not include the statistical and rating information required by subsections (d) and (e) of this section is not a proper filing, and will be returned to the filing insurer or organization.

(d) The following information must be included in policy form, rule, and rate filings:

- (1) A detailed list of the rates, rules, and policy forms filed, accompanied by a list of those superseded; and
- (2) A detailed description, properly referenced, of all changes in policy forms, rules, and rates, including the effect of each change.

(e) All policy form, rule, and rate filings that are based on statistical data must be accompanied by properly identified information, including but not limited to the following:

- (1) North Carolina earned premiums at the actual current rate level and losses and loss adjustment expenses on both paid and incurred bases, without trending or other modification for the experience period, including the loss ratio anticipated at the time the rates were promulgated for the experience period;
- (2) Credibility factor development and application;
- (3) Loss development factor derivation and application on both paid and incurred bases and in both numbers and dollars of claims;
- (4) Trending factor development and application;
- (5) Changes in premium base resulting from rating exposure trends;
- (6) Limiting factor development and application;
- (7) Premium dollar loss and expense exhibit;
- (8) Percent rate change;
- (9) Final proposed rates;
- (10) Investment income from loss reserves and unearned premium reserves;
- (11) Identification of applicable statistical plans and programs and a certification of compliance with them;
- (12) Investment earnings on capital and surplus;
- (13) Level of capital and surplus needed to support premium writings without endangering the solvency of the insurer; and
- (14) Such other information as may be specifically required by the Commissioner.

(f) It is unlawful for an insurer to charge or collect, or attempt to charge or collect, any premium for insurance except in accordance with filings made with the Commissioner under this section and Article 13C of this Chapter.

"<58-481. Provision for marketing facilities.--(a) Upon the request of any licensed individual fire and casualty agent, the Commissioner may, within 20 days after receipt of the request,

appoint that agent to represent a licensed insurer for the kinds of insurance for which the insurer is writing and for which the agent is licensed to sell.

(b) the insurer to which the agent is assigned may limit the agent's authority to bind the insurer on new policies, subject to evaluation by the insurer of the risk.

(c) The Commissioner may deny the agent's request if he finds any of the following:

- (1) The agent has not shown that he has been conducting his fire and casualty insurance business in the same community for at least two years;
- (2) The agent has not shown that he has written a gross premium volume during the 25 months next preceding the date of his application of at least fifty thousand dollars (\$50,000) from fire and casualty insurance;
- (3) The agent has not shown that the number of insureds served by him during the 25 months next preceding the date of his application was 100 or more;
- (4) The agent has not shown a growth in insureds served and premium volume during his years of service as an agent;
- (5) The agent has not shown that he has made available to insureds either premium financing or any other plan for deferred premium payments;
- (6) The agent has not shown that the public interest requires that the kind of insurance the agent is licensed to write is not and should be available to the insurance market served by the agent.

(d) This section does not apply to motor vehicle insurance.

"<58-482. Financial disclosure; rate modifications;

reporting requirements--(a) The Commissioner may adopt rules that require each insurer subject to this Article to report its premiums, loss and loss adjustment expense experience, investment earnings, administrative expenses, and other data that he may require, for kinds of insurance and classes of risks that he designates. These reports are in addition to financial or other statements required by Article 2 of this Chapter.

(b) The Commissioner may designate one or more rating organizations or advisory organizations to gather and compile this experience and data.

(c) Whereas the provisions enacted by the General Assembly in 1986 regarding modifications in the North Carolina civil justice system will have both a prospective and retrospective effect upon the loss experience of insurers subject to this Article, the Commissioner is directed to review rates in effect on and after the effective date of this section and, where appropriate, require modification of those rates.

(d) Each insurer subject to this Article shall record the experience and data referred to in subsection (a) of this section arising from actions or claims filed against its insureds on and

after the effective date of this section. This experience and data shall be reported to the Commissioner by January 1, 1988; this report shall be on a form prescribed by the Commissioner reflecting the experience and data for the one year period beginning on the effective date of this section. Subsequently, the experience and data shall be reported to the Commissioner by January 1 of each year for each one year period beginning on the anniversary of the effective date of this section.

(e) Beginning March 1, 1988, and annually thereafter, the Commissioner shall report to the General Assembly the effects, if any, of changes in North Carolina statutory law on the experience of insurers subject to this section.

"<58-483. Penalties; restitution.--In addition to criminal penalties for acts declared unlawful by this Article, any violation of this Article subjects an insurer to revocation or suspension of its certificate of authority, or monetary penalties or payment of restitution as provided in G.S. 58-9.7.

Sec. 2. G.S. 58-131.53(b), G.S. 58-131.56, and G.S. 58-131.59 are repealed.

Sec. 3. G.S. 58-131.38(1) is amended by rewriting the proviso to read:

"provided, however, that regional or countrywide expense or loss experience and other regional or countrywide data may be considered only when credible North Carolina expense or loss experience or other date is not available."

Sec. 4. G.S. 58-131.39 is amended by adding a new subsection to read:

(d) This section and G.S. 58-480 shall be construed in pari materia."

Sec. 5. G.S. 58-54.4(11) is amended by rewriting the heading and first phrase to read:

"(11) Unfair Claim Settlement Practices.--Committing or performing with such frequency as to indicate a general business practice of any of the following: Provided, however, that no violation of this subsection shall of itself be deemed to create any cause of action in favor of any person other than the Commissioner".

Sec. 6. G.S. 58-248.33(b)(1)e is rewritten to read:

"e. Any other motor vehicle insurance or financial responsibility limits in the amounts required by any federal law or federal agency regulation; by any law of this State; or by any rule duly adopted under General Statutes Chapter 150B or by the North Carolina Utilities Commission."

Sec. 7. G.S. 58-54.4(7) is amended by adding the following subdivisions:

- "c. Making or permitting any unfair discrimination between or amount individuals or risks of the same class and of essentially the same hazards by refusing to issue, refusing to renew, cancelling, or limiting the amount of insurance coverage on a property or casualty risk because of the geographic location of the risk, unless:
 - (1) The refusal or limitation is for a business purpose that is not a mere pretext for unfair discrimination, or
 - (2) The refusal, cancellation, or limitation is required by law.
- d. Making or permitting any unfair discrimination between or amount individuals or risks of the same class and of essentially the same hazards by refusing to issue, refusing to renew, cancelling, or limiting the amount of insurance coverage on a residential property risk, or the personal property contained therein, because the age of the residential property, unless:
 - (1) The refusal or limitation is for a business purpose that is not a mere pretext for unfair discrimination, or
 - (2) The refusal, cancellation, or limitation is required by law."

Sec. 8. G.S. 58-173.2 is amended by adding a new subsection to read:

"(3a) 'Crime insurance' means insurance against losses resulting from robbery, burglary, larceny, and similar crimes, and may include broad form personal theft insurance, mercantile open stock insurance, mercantile robbery and mercantile safe burglary insurance, storekeepers burglary and robbery insurance, office burglary and robbery insurance, and may include business interruption insurance as the Commissioner may designate; the term does not include automobile insurance and losses resulting from embezzlement."

Sec. 9. G.S. 58-173.8(b) is amended by inserting "or crime insurance, or both," between "property insurance" and "for a".

Sec. 10. G.S. 58-173.20, as found in the 1985 Supplement, is amended by inserting "or crime insurance policies, or both" immediately after "basic property insurance policies".

Sec. 11. G.S. 58-173.17 is amended by adding:

"As used in this Article, 'crime insurance' means insurance against losses resulting from robbery, burglary, larceny, and similarly crimes, and may include broad form personal theft insurance, mercantile open

stock insurance, mercantile robbery and mercantile safe burglary insurance, storekeepers burglary and robbery insurance, office burglary and robbery insurance, and may include business interruption insurance as the Commissioner may designate; the term does not include automobile insurance and losses resulting from embezzlement."

Sec. 12. G.S. 58-173.2(5) is amended by inserting "the Federal Manufactured Home Construction and Safety Standards, any predecessor or successor federal or state construction or safety standards, and any further construction of safety standards promulgated by the association and approved by the Commissioner, or" immediately before "the North Carolina Uniform Residential Building Code" in each place reference to that Code appears, except in the proviso at the end of the subsection.

Sec. 13. General Statute Chapter 58 is amended by adding a new Article to read:

"Article 39.

"Local Government Risk Pools.

"<58-490. Short title; definition.--This Article shall be known and may be cited as the Local Government Risk Pool Act. As used in this Article, "local government" means any county or municipal corporation located in this State.

"<58-491. Local government pooling of property, liability, and workers' compensation coverages.--In addition to other authority granted pursuant to Chapters 153A and 160A of the General Statutes, two or more local governments may enter into contracts or agreements pursuant to this Article for the joint purchasing of insurance or to pool retention of their risks for property losses and liability claims and to provide for the payment of such losses of or claims made against any member of the pool on a cooperative or contract basis with one another, or may enter into a trust agreement to carry out the provisions of this Article. In addition to other authority granted pursuant to Chapters 153A and 160A of the General Statutes, two or more local governments may enter into contracts or agreements pursuant to this Article to establish a separate workers' compensation pool to provide for the payment of workers' compensation claims pursuant to Chapter 97 of the General Statutes or to establish pools providing for life or accident and health insurance for their employees on a cooperative or contract basis with one another; or may enter into a trust agreement to carry out the provisions of this Article. A workers' compensation pool established pursuant to this Article may only provide coverage for workers' compensation, employers' liability, and occupational disease claims.

"<58-492. Board of trustees.--(a) Each pool will be operated by a board of trustees consisting of at least five persons who are elected officials or employees of local

governments within this State. The board of trustees of each pool will:

- (1) Establish terms and conditions of coverage within the pool, including underwriting criteria and exclusions of coverage;
 - (2) Ensure that all claims are paid promptly;
 - (3) Take all necessary precautions to safeguard the assets of the pool;
 - (4) Maintain minutes of its meeting and make those minutes available to the Commissioner;
 - (5) Designate an administrator to carry out the policies established by the board of trustees and to provide day to day management of the group and delineate in written minutes of its meetings the areas of authority it delegates to the administrator; and
 - (6) Establish guidelines for membership in the pool.
- (b) The board of trustees may not:
- (1) Extend credit to individual members for payment of a premium, except pursuant to payment plans approved by the Commissioner.
 - (2) Borrow any monies from the pool or in the name of the pool, except in the ordinary course of business, without first advising the Commissioner of the nature and purpose of the loan and obtaining prior approval from the Commissioner.

"<58-493. Contract.--A contract or agreement made pursuant to this Article must contain provisions:

- (1) For a system or program of loss control;
- (2) For termination of membership including either:
 - (a) Cancellation of individual members of the pool by the pool; or
 - (b) Election by an individual member of the pool to terminate its participation;
- (3) Requiring the pool to pay all claims for which each member incurs liability during each member's period of membership, except where a member has individually retained the risk, where the risk is not covered, and except for amount of claims above the coverage provided by the pool.
- (4) For the maintenance of claim reserves equal to known incurred losses and loss adjustment expenses and to an estimate of incurred but not reported losses;
- (5) For a final accounting and settlement of the obligations of or refunds to a terminating member to occur when all incurred claims are concluded, settled, or paid;
- (6) That the pool may establish offices where necessary in this State and employ necessary staff to carry out the purposes of the pool;

- (7) That the pool may retain legal counsel, actuaries, claims adjusters, auditors, engineers, private consultants, and advisors, and other persons as the board of trustees or the administrator deem to be necessary;
- (8) That the pool may make and alter bylaws and rules pertaining to the exercise of its purpose and powers;
- (9) That the pool may purchase, lease, or rent real and personal property it deems to be necessary; and
- (10) That the pool may enter into financial services agreements with financial institutions and that it may issue checks in its own name.

"<58-494. Termination.--A pool or a terminating member must provide at least 90 days' written notice of the termination or cancellation. A workers' compensation pool must notify the Commissioner of the termination or cancellation of a member within 10 days after notice of termination or cancellation is received or issued.

"<58-495. Audit.--Each pool must be audited annually at the expense of the pool by a certified public accounting firm, with a copy of the report submitted to the governing body or chief executive officer of each member of the pool and to the Commissioner. The board of trustees of the pool must obtain an appropriate actuarial evaluation of the loss and loss adjustment expense reserves of the pool, including an estimate of losses and loss adjustment expenses incurred but not reported. The Commissioner must examine each pool once every three years. The costs of such examination expenses will be paid by the pool that is subject to the examination. The Commissioner may examine a pool earlier than three years after a previous examination if he has reason to believe that the pool is insolvent or financially impaired.

"<58-496. Insolvency or impairment of pool.--(a) If, as a result of the annual audit or an examination by the Commissioner, it appears that the assets of a pool are insufficient to enable the pool to discharge its legal liabilities and other obligations, the Commissioner must notify the administrator and the board of trustees of the pool of the deficiency and his list of recommendations to abate the deficiency, including a recommendation not to add any new members until the deficiency is abated. If the pool fails to comply with the recommendations within 60 days after the date of the notice, the Commissioner must notify the chief executive officers or the governing bodies of the members of the pool, the Governor, the President of the Senate, and the Speaker of the House of Representatives that the pool has failed to comply with the recommendations of the Commissioner.

(b) If a pool is determined to be insolvent, financially impaired, or is otherwise found to be unable to discharge its legal liabilities and other obligations, each pool contract will provide that the members of the pool shall be assessed on a pro

rata basis as calculated by the amount of each member's average annual contribution in order to satisfy the amount of deficiency. The assessment may not exceed the amount of each member's average annual contribution to the pool.

"<58-497. Immunity of administrators and boards of trustees.--There is no liability on the part of and no cause of action arises against any board of trustees established or administrator appointed pursuant to G.S. 58-492, their representatives, or any pool, its members, or its employees, agents, contractors, or subcontractors for any good faith action taken by them in the performance of their powers and duties in creating or administering any pool under this Article.

"<58-498. Pools not covered by guaranty associations or solvency funds.--The provisions of Articles 17B and 17C of this Chapter and of Article 3 of General Statute Chapter 97 do not apply to any risks retained by local governments pursuant to this Article."

Sec. 14. Article 13C of Chapter 58 of the General Statutes is amended by adding a new section to read:

"<58-131.61. Good faith immunity for operation of market assistance programs.--There is no liability on the part of and no cause of action of any nature arises against any director, administrator, or employee of a market assistance program, or the Commissioner or his representatives, for any acts or omissions taken by them in creation or operation of a market assistance program. The immunity established by this section does not extend to willful neglect, malfeasance, bad faith, fraud, or malice that would otherwise make an act or omission actionable."

Sec. 15. Article 13C of Chapter 58 of the General Statutes is amended by adding a new section to read:

"<58-131.62. CGL extended reporting.--Any policy for commercial general liability coverage wherein the company shall offer, and the insured may elect to purchase, an extended reporting period for claims arising during the expiring policy period shall provide:

- (1) That in the event of a cancellation, there shall be a 30 day period during which the insured may elect to purchase coverage for the extended reporting period;
- (2) That the limit of liability in the policy aggregate for the extended reporting period shall be one hundred percent (100%) of the expiring policy aggregate; and
- (3) That the company will provide the following loss information to the first named insured within 30 days of the insured's request or with any notice of cancellation or nonrenewal:
 - (a) All information on closed claims including date and description of occurrence, and amount of payments, if any;

- (b) All information on open claims including date and description of occurrence, amount of payment, if any and amount of reserves, if any;
- (c) All information on notices of occurrence including date and description of occurrence and amount of resources, if any."

Sec. 16. G.S. 58-27.22. is amended:

(a) By deleting the words, "county or municipality", "counties and municipalities", "counties or municipalities", and "municipality and county" from the section, and by substituting the words "political subdivision" or "political subdivisions" as grammatically appropriate; and

(b) By adding the following, at the end:

"For purposes of this section, the term 'political subdivision' includes any county, city, town, incorporated village, sanitary district, metropolitan water district, county water and sewer district, water and sewer authority, hospital authority, parking authority, special airport district, airport authority, soil and water conservation district created pursuant to G.S. 139-5, area mental health, mental retardation and substance abuse authority as described in G.S. 122C-117, county and city boards of education and school administrative units, and all other bodies or agencies provided for by or established pursuant to Chapters 153A, 160A, and 160B of the General Statutes."

Sec. 17. Rule 54. Judgments. of G.S. 1A-1 is amended by adding a new subsection to read:

"(a1) All judgments providing for the payment of punitive damages shall provide that the plaintiff in the case shall receive any amount up to one hundred thousand dollars (\$100,000) and any amount over one hundred thousand dollars (\$100,000) shall be paid to the Clerk of the Court in which the action is pending. The Clerk of Court shall promptly transmit that amount to the Treasurer of the State for deposit into the General Fund of the State."

Sec. 18. Rule 54. Judgments. of G.S. 1A-1 is amended by adding a new subsection to read:

"(a2) No judgment shall be rendered that allows a plaintiff in any civil action to recover damages for noneconomic losses, in an amount that exceeds two hundred fifty thousand dollars (\$250,000), to compensate for pain, suffering, inconvenience, distress, or any other damages when any of these damages cannot be proven to have a specific economic value."

Sec. 19. Chapter 1B of the General Statutes is amended by adding a new Article to read:

"Article 4.
"Joint Liability.

"**1B-9. Definitions.**--As used in this Article, unless the context requires otherwise, the following words have the following meanings:

"(1) 'Defendant' means a person not immune from suit who is claimed to be liable because of fault to any person seeking recovery.

"(2) 'Fault' means any actionable breach of legal duty, act, or omission proximately causing or contributing to injury or damages sustained by a person seeking recovery, including, but not limited to, negligence in all its degrees, contributory negligence, assumption of risk, strict liability, breach of express or implied warranty of a product, products liability, and misuse, modification, or abuse of a product.

"(3) 'Plaintiff' means any person seeking damages or reimbursement on his own behalf, or on behalf of another for whom he is authorized to act as legal representative.

"**1B-10. Recovery.**--A plaintiff may recover damages from any group of defendants whose fault has caused him damages. However, no defendant is liable to any person seeking recovery for any amount in excess of the proportion of fault attributable to that defendant. This section is not intended to modify or in any way affect the doctrine of contributory negligence found in G.S. 1-139 and G.S. 1A-Rule 8.

"**1B-11. Itemized verdicts.**--(a) The Court may upon its own motion, and when requested by any party shall, direct the jury to find separate special verdicts determining the total amount of damages sustained and the percentage or proportion of fault attributable to each defendant.

(b) In a matter tried to the Court alone, upon motion of any party, the Court shall determine the total amount of the damages sustained and the percentage or proportion of fault attributable to each defendant.

"**1B-12. Damages.**--The maximum amount for which a defendant may be liable to a plaintiff is the percentage or proportion of the damages equivalent to the percentage or proportion of fault attributed to that defendant.

"**1B-13. Parties.**--A plaintiff or any defendant may join as parties any persons who may have caused or contributed to the injury or damage for which the recovery is sought, for the purpose of having determined their respective proportions of fault.

"1B-14. Releases.--A release given to one or more defendants by a plaintiff does not discharge any other defendant unless the release provides for that discharge.

"1B-15. Effect of this Article.--Nothing in this Article affects or impairs any common law or statutory immunity from liability or impairs any right to indemnity or contribution arising from statute, contract, or agreement."

Sec. 20. Articles 1 and 2 of Chapter 1B of the General Statutes are repealed.

Sec. 21. Chapter 160A of the General Statutes is amended by adding a new Article to read:

"ARTICLE 26
"POLITICAL SUBDIVISION TORT CLAIMS ACT

"<160A-590. Short Title.--This Article may be referred to as the Political Subdivision Tort Claims Act.

"<160A-591. Definitions.--Unless the context requires otherwise, the following terms shall have the meanings indicated:

- (1) 'Employee' means any present or former employee, officer, involuntary servant, or agent of a political subdivision; any member or employee, whether paid or voluntary, of a volunteer fire department or rescue squad, or any other public or private entity that provides fire or rescue services; physicians or other health care professionals acting pursuant to contracts with health departments; or any other person while acting within the scope of his employment for any political subdivision, whether paid or voluntary.
- (2) 'Political subdivision' shall include any county, city, town, incorporated village, sanitary district, metropolitan water district, county water and sewer district, water and sewer authority, hospital authority, parking authority, special airport district, airport authority, soil and water conservation district created pursuant to G.S. 139-5, fire district, volunteer or paid fire department, rescue squads, area mental health boards, area mental health, mental retardation and substance abuse authority as described in G.S. 122C-117, domiciliary home community advisory committees, county and district boards of health, nursing home advisory committees, county boards of social services, local school administrative units, local boards of education, community colleges and

technical institutes, and all other persons, bodies, or agencies regulated by Chapters 108A, 115C, 115D, 118, 122C, 130A, 131A, 131D, 131E, 153A, 160A, and 160B of the General Statutes.

- (3) 'Scope of employment' means scope of office, employment, service, agency or authority.
- (4) 'Tort' means any action for damages for personal injuries or property damage arising out of the negligence of any political subdivision or of any employee of a political subdivision.

"<160A-592. Claims.--(a) All claims against any political subdivision or against any employee for personal or property damages arising out of an act of negligence shall be filed in the Superior Court of the County in which the political subdivision is located. As a condition precedent to the filing of an action against the political subdivision or employee, the claimant shall give notice to the governing body of the political subdivision against whom the claim is being filed within 180 days of the event out of which the claim arose.

(b) If the trier of fact finds that there was negligence on the part of the employee of the political subdivision while acting within the scope of his employment under circumstances where the political subdivision, if a private person, would be liable to the claimant in accordance with the laws of North Carolina, and that those circumstances were the proximate cause of the injury claimed, and that there was no contributory negligence on the part of the claimant or the person in whose behalf the claim is asserted, the trier of fact shall determine the amount of damages which the claimant is entitled to be paid.

(c) The Court shall issue a judgment directing the payment of the damages by the political subdivision, but in no event shall the amount of damages awarded exceed the sum of one hundred thousand dollars (\$100,000) cumulatively to all claimants on account of injury and damage to any one person.

"<160A-593. Appeal to Court of Appeals to act as supersedeas.--The appeal from the decision of the Superior Court to the Court of Appeals shall act as a supersedeas and the political subdivision shall not be required to make payment of any judgment until the questions at issue shall have been finally determined.

"<160A-594. Settlement of Claims.--(a) The governing bodies of political subdivisions covered by this Article may settle, on a case by case basis, any claims, except the claims of minors, in an amount of twenty-five thousand dollars (\$25,000) or less without an action being filed in Superior Court. The political subdivision may make settlements by agreement for claims in excess of twenty-five thousand dollars (\$25,000) and claims of minors or

persons non sui juris, provided that these settlements have been reviewed and approved by the Court.

"<160A-595. Limitations on claims.--(a) All claims against political subdivisions arising out of alleged tortious acts shall be barred unless an action is filed in Superior Court within two years after the event out of which the claim arose.

(b) No claims or actions shall arise out of the following 'governmental' functions of the political subdivisions:

- (1) making and enforcing ordinances;
- (2) preventing crime and operating a police force;
- (3) preserving the public health;
- (4) preventing or suppressing fires and operating a paid or voluntary fire department;
- (5) providing services to the poor;
- (6) providing educational services;
- (7) providing animal control services;
- (8) controlling and regulating bus companies;
- (9) discharging public employees;
- (10) maintaining airports;
- (11) operating and maintaining libraries;
- (12) installing and maintaining traffic signal lights
- (13) installing and maintaining systems providing electricity for street lighting
- (14) operating and maintaining of parks
- (15) providing garbage disposal services (where the service is operated on a nonprofit basis);
- (16) performing duties imposed on a political subdivision by statute; and
- (17) performing any other actions or functions in exercise of police power, or judicial, discretionary, or legislative authority, conferred by their charters or by statute, and when discharging a duty imposed solely for the public benefit.

(c) Political subdivisions shall not pay punitive damages.

"<160A-596. Contributory negligence a matter of defense; burden of proof.--Contributory negligence on the part of the claimant or the person in whose behalf the claim is asserted shall be deemed to be a matter of defense on the part of the political subdivision against which the claim is asserted, and that political subdivision shall have the burden of proving that the claimant or the person in whose behalf the claim is asserted was guilty of contributory negligence."

Sec. 22. All local laws and local acts in conflict with section 21 of this Act are repealed.

Sec. 23. Rule 54. Judgments. of G.S. 1A-1 is amended by adding a new subsection to read:

"(d)(1)a. In any action for damages for personal injury or wrongful death, whether in tort or contract, in which liability is admitted or determined by the trier of fact and damages are awarded to compensate the plaintiff for losses sustained, the Court shall reduce the amount of the award by the total of all amounts paid to the plaintiff from all collateral sources which are available to him.

b. Upon a finding of liability and an awarding of damages by the trier of fact, the Court shall receive evidence from the plaintiff and other appropriate persons concerning the total amounts of collateral sources which have been paid for the benefit of the plaintiff or are otherwise available to him.

c. The Court shall also take testimony of any amount which has been paid, contributed, or forfeited by, or on behalf of, the plaintiff or members of his immediate family to secure his right to any collateral source benefit which he is receiving as a result of his injury, and shall offset any restriction in the award by those amounts.

d. Notice shall be given to all collateral sources of the evidentiary hearings provided for in this subsection and failure of the collateral source to join the action will bar any future recovery from either the plaintiff or the defendant by subrogation.

e. In the case where the plaintiff has made a demand for payment from a collateral source but that payment has not been made at the time the judgment is awarded, the Court shall provide for the amount of the potential setoff of the judgment required by this subsection to be placed in escrow until the collateral source has made payment to the plaintiff. If the collateral source makes payment, then the amount held in escrow shall be returned to the defendant. If the collateral source does not make payment, then the amount held in escrow shall not be setoff and shall be paid to the plaintiff. The Court shall hold an evidentiary hearing on the disposition of the funds held in escrow no later than one year after the judgment is rendered in the case, unless petitioned by either party prior to that date.

"(2) For purposes of this subsection, payments from collateral sources includes payments made to the plaintiff, or on his behalf, by or pursuant to:

a. The United States Social Security Act; any federal, state, or local income disability act; or any other public programs providing medical expenses, disability payments, or other similar benefits.

b. Any health, sickness, or income disability insurance; automobile accident insurance that provides health benefits or income disability coverage; and any other similar insurance benefits, except life insurance benefits available to the plaintiff, whether purchased by him or provided by others.

c. Any contract or agreement of any group, organization, partnership, or corporation to provide, pay for, or reimburse the costs of hospital, medical dental, or other health care services.

d. Any contractual or voluntary wage continuation plan provided by employers or any other system intended to provide wages during a period of disability.

"(3) In the event that the fees for legal services provided to the plaintiff are based on a percentage of the amount of money awarded to the plaintiff, that percentage shall be based on the net amount of the award as reduced by the amounts of collateral sources and as increased by insurance premiums paid."

Sec. 24. Chapter 1 of the General Statutes is amended by adding a new Article to read:

"Article 23A
"Structured Awards.

"1-246.1. Structured Awards.--In any civil action in which the trier of fact or the Court makes an award which provides compensation to the plaintiff for future losses, payment of amounts intended to compensate for these future losses shall be made by one of the following means:

(1) The defendant may make a lump-sum payment for all damages so assessed, with future losses and reduced to present value; or

(2) Subject to the provisions of this Article, the Court shall, at the request of either party, unless the Court determines that manifest injustice would result to any party, enter a judgment ordering the damages for future losses to be paid in whole or in part by periodic payments rather than by lump-sum payment.

"1-246.2. Findings by Court.--(a) In entering a judgment ordering the payment of future losses by periodic payments, the Court shall make a specific finding of the dollar amount of periodic payments which will compensate the judgment creditor for the future losses after offset for collateral sources.

(b) The total dollar amount of the periodic payments shall equal the dollar amount of all future losses before any reduction to present value, less any attorney's fees payable from future losses in accordance with G.S. 1-246.6.

(c) The period of time over which the periodic payments shall be made is the period of years determined by the trier of fact in arriving at its itemized verdict, and shall not be extended if the plaintiff lives beyond the determined period.

(d) The judgment providing for payment of future losses by periodic payments shall specify:

- (1) The recipient or recipients of the payments;
- (2) The dollar amounts of the payments;
- (3) The interval between payments; and
- (4) The number of payments or the period of time over which the payments shall be made.

(e) If the plaintiff has been awarded damages to be discharged by periodic payments and the plaintiff dies prior to the termination of the period of years during which periodic payments are to be made, the remaining liability of the defendant shall be paid to the estate of the plaintiff in a lump-sum equal to the present value of the payments that would have been paid to the plaintiff had he lived.

(f) The Court may order that the payments be equal or vary in amount, depending upon the needs of the plaintiff.

"<1-246.3. Bond or security required.--(a) As a condition to authorizing periodic payments of future losses, the Court shall require the defendant to post a bond or security or annuity contract to assure full payment of periodic payments awarded by judgment.

(b) A bond or annuity contract is not adequate unless it is written by an insurance company licensed to do business in this State or by an insurance company rated A by Best's.

(c) If the Court finds that the defendant is unable to adequately assure full payment of the periodic payments when due, the Court shall order that all damages be paid to the plaintiff in a lump sum pursuant G.S. 1-246.1(1).

(d) No bond may be canceled or be subject to cancellation unless at least 60 days' advanced notice is filed with the Court and the judgment creditor.

(e) Upon termination of periodic payments, the Court shall order the return of the security, or so much as remains, to the judgment debtor. The Court may, in its discretion, return all or a portion of the security to the judgment debtor prior to termination of the periodic payments if the security or a portion of the security is no longer necessary to adequately assure full payment of the remaining periodic payments.

"<1-246.4. Failure to make periodic payments.--(a) In the event that the Court finds that the judgment debtor has exhibited a continuing pattern of failing to make the required periodic payments in a timely manner, the Court shall:

- (1) Order that all remaining amounts of the award be paid by lump sum within 30 days after entry of the order;
- (2) Order that, in addition to the required periodic payments, the judgment debtor pay the plaintiff all damages caused by the failure to make periodic payments in a timely manner, including court costs and attorney's fees; or

(3) Enter other orders or sanctions as appropriate to protect the judgment creditor.

(b) If the Court finds that the judgment debtor may be insolvent or that there is a substantial risk that the judgment debtor may not have the financial responsibility to pay all amounts due and owing the judgment creditor, the court may:

- (1) Order additional security;
- (2) Order that the balance of payments due be placed in trust for the benefit of the plaintiff;
- (3) Order that all amounts of the award be paid by lump sum within 30 days after entry of the order; or
- (4) Order any other protection necessary to assure the payment of the remaining balance of the judgment.

(c) Periodic payments shall be subject to modification only as specified in this Article.

"<1-246.5. Attorney's fees.--(a) The plaintiff's attorney's fees, if payable from the judgment, shall be based on the total judgment, adding all amounts awarded for past and future losses.

(b) The attorney's fee shall be paid from past and future losses in the same proportion.

(c) If the plaintiff has agreed to pay his attorney's fees on a contingency fee basis, the plaintiff shall be responsible for paying the agreed percentage calculated solely on the basis of that portion of the award not subject to periodic payments. The remaining unpaid portion of the attorney's fees shall be paid in a lump sum by the defendant, who shall receive credit against future payments for this amount. However, the credit against each future payment is limited to an amount equal to the contingency fee percentage of each periodic payment.

(d) Any provision of this section may be modified by the agreement of all interested parties.

"<1-246.6. Agreement of parties.--Nothing in this Article shall preclude any other method of payment of awards, if the method is consented to by the parties."

Sec. 25. G.S. 97-10.1 is designated as subsection (a).

Sec. 26. G.S. 97-10.1 is amended by adding a new subsection to read:

"(b) No design professional who is retained to perform services on a construction project, nor any employee of a design professional who is assisting or representing the design professional on the site of the construction project, shall be liable for any injury to an employee of an owner, principal contractor, intermediate contractor, subcontractor, or any other employer when that employee is injured on the construction site and is subject to the provisions of this Article, unless the injury is a result of the design professional's negligent preparation of designs, plans, or specifications, or unless the

injury is a result of the willful, wanton, or malicious conduct towards of the design professional or any of his employees. For purposes of this subsection 'design professional' means a 'professional engineer' as defined in Chapter 89C of the General Statutes or an 'architect' as defined in Chapter 83A of the General Statutes."

Sec. 27. Section 26 of this act shall apply to injuries suffered on or after the effective date of this act and shall not affect pending litigation.

Sec. 28. The first two sentences of G.S. 6-21.5 are rewritten to read: "In any civil action, defense to a civil action, or special proceeding, the Court, upon the motion of the prevailing party, shall award costs and reasonable attorney's fees in connection with the civil action, defense, or special proceeding to the prevailing party against the nonprevailing party, his attorney, or both, if the Court finds that the action was not well grounded in fact or was not warranted by existing law of North Carolina nor supported by a good faith argument for extension, modification, or reversal of existing law. If the Court does not award attorney's fees in the case, it shall make finding of fact and law, on the record, as to its reasons for not granting attorney's fees."

Sec. 29. The fourth sentence of G.S. 1A-1, Rule 11(a) is rewritten to read: "The signature of an attorney constitutes a certificate by him that he has read the pleading; that he has conducted a reasonable, independent, preliminary investigation into the facts and law alleged in the pleading and that there is good ground to support the filing of the pleading; and that the pleading is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needlessly increase in the costs of litigation. If a pleading, motion, or other paper is signed in violation of this rule, the Court, upon motion or upon its own initiative, shall impose upon the attorney who signed it, a represented party, or both, an appropriate sanction, which may include an order to pay to the other party or parties the amount of the reasonable expenses incurred because of the filing of the pleading, motion, or other paper including a reasonable attorney's fee and which may include referral of the matter to the North Carolina State Bar for investigation and action."

Sec. 30. G.S. 130A-294 is amended by adding a new subdivision to read:

"(j) The Commission shall adopt, and the Department shall enforce, rules for financial responsibility (including requirements for sufficient availability of funds for facility closure and post-closure monitoring and corrective measures, and for potential liability for sudden and non-sudden releases) that shall permit the use of insurance,

assets, third-party guarantees, guarantees by corporate parents, irrevocable letters of credit, trusts, surety bonds, or any other financial device, or any combination of the foregoing, shown to provide protection substantially equivalent to the protection that would be provided by insurance. The owner or operator of a hazardous waste facility shall be permitted to use insurance, assets, third-party guarantees, guarantees by corporate parents, irrevocable letters of credit, trusts, surety bonds, or any other financial device or other financial device, or any combination of the foregoing, shown to provide protection substantially equivalent to the protection that would be provided by insurance. The rules shall provide that a copy of any filing to meet the financial responsibility requirements shall be transmitted by the Department to the State Treasurer, or his designee; provided, that this requirement of transmittal to the State Treasurer shall not apply to any financial responsibility filing that is based solely on insurance. Upon receipt, the State Treasurer, or his designee, shall review the financial responsibility filing to ensure that the mechanisms proposed in the financial responsibility filing provide financial protection substantially equivalent to the protection that would be provided by insurance. Upon completion of the review of the filing, the State Treasurer shall transmit to the Department a written report containing the recommendations and conclusions by the State Treasurer as to the acceptability of the filing, including recommended changes in the filing to ensure that the mechanisms proposed in the filing provide financial protection substantially equivalent to the protection that would be provided by insurance. The Department shall, in evaluating the acceptability of the financial responsibility filing, be guided by the written report received from the State Treasurer. After approval by the Department of the financial responsibility filing, the mechanisms of the financial responsibility filing as approved shall not be modified, reduced, withdrawn, terminated, or altered in any way without the prior review and written approval of the Department."

Sec. 31. G.S. 143-215.3(a)(15) is amended by adding the following at the end:

"In developing and adopting standards concerning financial responsibility for underground tanks used in the storage of hazardous substances or oil, The Commission shall adopt, and the Department shall enforce, rules for financial responsibility (including requirements for sufficient availability of funds for facility closure and post-closure monitoring and corrective measures, and for potential liability for sudden and non-sudden releases) that shall permit the use of insurance, assets, third-party guarantees,

guarantees by corporate parents, irrevocable letters of credit, trusts, surety bonds, or any other financial device, or any combination of the foregoing, shown to provide protection substantially equivalent to the protection that would be provided by insurance. The owner or operator of a hazardous waste facility shall be permitted to use insurance, assets, third-party guarantees, guarantees by corporate parents, irrevocable letters of credit, trusts, surety bonds, or any other financial device or other financial device, or any combination of the foregoing, shown to provide protection substantially equivalent to the protection that would be provided by insurance. The rules shall provide that a copy of any filing to meet the financial responsibility requirements shall be transmitted by the Department to the State Treasurer, or his designee; provided, that this requirement of transmittal to the State Treasurer shall not apply to any financial responsibility filing that is based solely on insurance. Upon receipt, the State Treasurer, or his designee, shall review the financial responsibility filing to ensure that the mechanisms proposed in the financial responsibility filing provide financial protection substantially equivalent to the protection that would be provided by insurance. Upon completion of the review of the filing, the State Treasurer shall transmit to the Department a written report containing the recommendations and conclusions by the State Treasurer as to the acceptability of the filing, including recommended changes in the filing to ensure that the mechanisms proposed in the filing provide financial protection substantially equivalent to the protection that would be provided by insurance. The Department shall, in evaluating the acceptability of the financial responsibility filing, be guided by the written report received from the State Treasurer. After approval by the Department of the financial responsibility filing, the mechanisms of the financial responsibility filing as approved shall not be modified, reduced, withdrawn, terminated, or altered in any way without the prior review and written approval of the Department.

Sec. 32. It is the intention of the General Assembly that the appropriate agencies of the State seek and maintain to the maximum possible extent the designation under federal law as the entity primarily responsible for the interpretation and enforcement of laws governing solid and hazardous waste substances and oils located within the State. To that end, nothing in sections 27 and 28 of this act shall be interpreted to be inconsistent with the provision of the applicable federal laws governing solid and hazardous waste facilities and underground storage tanks containing hazardous substances and oils, including, without limitation, the provisions of those federal laws concerning the designation of agencies of the State as being

primarily responsible for the interpretation and enforcement of those laws. It is the further intention of the General Assembly that the level of coverage required to be provided by the financial devices (or combination of financial devices) authorized by sections 30 and 31 of this act shall be the same as the coverage which is required, or which may in the future be required, for insurance alone.

Sec. 33. G.S. 55-19(a) is rewritten to read:

"(a) In addition to the indemnification provided for in G.S. 55-20 and G.S. 55-21, a corporation may in its charter or bylaws or by contract or resolution indemnify or agree to indemnify any one or more of its officers, directors, employees or agents against liability and litigation expense, including reasonable attorneys' fees, arising out of their status as such or their activities in any of the foregoing capacities. A corporation may likewise and to the same extent indemnify or agree to indemnify any person who, at the request of the corporation, is or was serving as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise."

Sec. 34. G.S. 55-19(b) is rewritten to read:

"(b) Notwithstanding the provisions of subsection (a) of this section, a corporation shall not indemnify or agree to indemnify any person against liability or litigation expense he may incur on account of his activities which were at the time taken known or believed by him to be clearly in conflict with the best interests of the corporation.

Sec. 35. G.S. 55-19(d) is amended by adding immediately after "in the specific case" the words "or as authorized or required under any charter or bylaw provision or by any applicable resolution or contract" and is further amended by deleting "as authorized in this section or in G.S. 55-20 or 55-21" and substituting "against such expenses".

Sec. 36. (a) Except as provided in subsections (b), (c), and (d) of this section, this act is effective upon ratification.

(b) Section 14 is effective March 10, 1986.

(c) Sections 1 (except for G.S. 58-482), 2, 4, 5, and 7 through 12, and 15 shall become effective August 1, 1986.

(d) Sections 17 through 29 shall become effective October 1, 1986 and shall apply to all actions, claims, or pleadings filed on or after that date.

APPENDIX H

REPORT TO 1986 SESSION OF GENERAL ASSEMBLY

June 5, 1986

The Honorable Robert B. Jordan III
President of the Senate

The Honorable Liston B. Ramsey
Speaker of the House of Representatives

On behalf of the members of the Commission we are pleased to present to you and the North Carolina General Assembly this interim report recommending one bill for consideration.

The Commission was charged by Chapter 792 of the 1985 Session Laws with studying and reporting on:

- (1) "The availability of professional and commercial liability and property insurance in the State and the factors causing and compounding diminutions in underwriting capacity.
- (2) "The underwriting and marketing practices of admitted and nonadmitted liability and property insurers and producers doing business in this State.
- (3) "Optional methods of risk management or risk sharing that may be utilized by the citizens of this State.
- (4) "The effect of diminished underwriting capacity in professional and commercial liability and property insurance on the economy of this State.
- (5) "Any other subjects deemed by the Commission to be relevant to this study."

The Commission began its work in October, 1985 and conducted eleven meetings, including five public hearings across the State, during which it solicited the suggestions of all sectors of the economic life of the State including insurance companies, insurance agents, businesses, professionals, political subdivisions, public service organizations, and citizens. The Commission considered pending legislation in other states and pending legislation on the federal level. The Commission worked closely with the Commissioner of Insurance, and his staff, as evidenced by the introduction of the legislation during the February, 1986 Special Session of the General Assembly.

As a result of the deliberations and hard work of the Commission, the attached draft legislation was approved by the Commission and recommended for introduction in the 1986 Session.

The Commission will continue its work and will make a final report to the 1987 Session of the General Assembly.

FOR THE COMMISSION

Senator Harold W. Hardison

Rep. John C. "Pete" Hasty

COCHAIRMEN

APPENDIX I

ANALYSIS OF CHAPTER 1027 OF THE 1985 SESSION LAWS

This Appendix is a section by section review of the of Chapter 1027 of the 1985 Session Laws as ratified by the General Assembly on July 16, 1986. Notes indicate which sections were recommended by this Commission.

Section 1. (a) Adds a new section, G.S. 58-124.31, that provides that the Bureau shall propose and the Commissioner shall promulgate rate classifications, schedules, or rules that he deems desirable and equitable to classify drivers for insurance policies. The Commissioner may modify the classifications, schedules, and rules.

(b) The Bureau shall propose and the Commissioner shall promulgate a Safe Driver Incentive Plan distinguishing among the different classes of safe and unsafe drivers. The Commissioner may modify the S.D.I.P. to provide for surcharges and discounts.

(c) All of these are subject to review under the Administrative Procedure Act and shall not bring about an increase or decrease in overall rate level.

(d) Upon the loss of a safe driver discount or imposition of a surcharge, the insurer shall notify the insured of the reasons for the loss of the discount or imposition of the surcharge.

(e) Records of convictions shall be obtained by the insurers at least annually.

(f) The Bureau may establish reasonable rules for the exchange of information among its members concerning insured's driving records.

(g) Knowing material misrepresentations by an insured subject him to cancellation of the policy, surcharge on the policy, or recovery of additional premium that would have been applied to the policy. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 2. Rewrites G.S. 58-124.20(d) which now reads:

"(d) On or before July 1 of each calendar year the Bureau shall submit to the Commissioner for the motor vehicle liability insurance subject to the provisions of this Article the experience, data, statistics, and information referred to in subsection (c) of this section and a rate review based on such data."

Subsection (c) of G.S. 58-124.20 now reads:

"(c) The Bureau shall maintain reasonable records, of the type and kind reasonably adapted to its method of operation, of the experience of its members and of the data, statistics or information collected or used by it in connection with the rates,

rating plans, rating systems, underwriting rules, policy or bond forms, surveys or inspections made or used by it." (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 3. Adds new subsections (g), (h), and (i) to G.S. 58-124.20. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Sections 3.1 and 4. Rewrite G.S. 124.22(b) so that it will read:

"(b) Except as provided in G.S. 58-125.32, whenever a Bureau rate is held to be unfairly discriminatory or excessive and no longer effective by order of the Commissioner issued under G.S. 58-124.21, the members of the Bureau, in accordance with the rules and regulations established and adopted by the governing committee, shall have the option to continue to use such rate for the interim period pending judicial review of such order, provided each such member shall place in escrow account the purportedly unfairly discriminatory or excessive portion of the premium collected during such interim period. Upon a final determination by the court, the Commissioner shall order the escrowed funds to be distributed appropriately, except that individual refunds that are five dollars (\$5.00) or less shall not be required. The court may also require that purportedly excess premiums resulting from an adjustment of premiums ordered pursuant to G.S. 58-124.21(b) be placed in such escrow account pending judicial review. The amounts escrowed hereunder shall bear interest at the prime rate as of the date such rates were put into effect."(THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 5. Adds a new section that (a) Makes a rate filing for nonfleet passenger motor vehicle insurance effective after a 60 day delay to allow the Commissioner to act. If he calls for a hearing on the proposed rate increase, there shall be a 30 day written notice of the hearing.

(b) At least 15 days before the hearing all parties shall attend a prehearing conference at which all issues that can be resolved shall be resolved.

(c) Hearings shall proceed without undue delay. The burden to prove the validity of the proposed rates rests with the proposers. The Commissioner may disregard evidence that could have been included in the rate filing but was not, unless that evidence is rebuttal evidence. Provides for the order of presenting evidence. Provides that the Bureau shall reimburse the Department for outside witnesses and court reporting service.

(d) Provides for orders by the Commissioner within 45 days of the end of the hearing.

(e) Prohibits the withholding of or the submission of false information necessary for the operation of this Article.(THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 5.1. Adds two new subdivisions to the section that sets forth the objects and functions of the North Carolina Rate Bureau.(THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 6. Amends G.S. 58-124.18(b) so that it will read:

(b) Each member of the Bureau writing any one or more of the above lines of insurance in North Carolina shall, as a requisite thereto, be represented in the Bureau and shall be entitled to one representative and one vote in the administration of the affairs of the Bureau. They shall, upon organization elect a governing committee which governing committee shall be composed of equal representation by stock and nonstock members. The governing committee, each of its subcommittees, and each special ad hoc committee of the Bureau shall also have as nonvoting members three persons who are not employed by or affiliated with any insurance company and who are appointed by the Governor, Lieutenant Governor, and Speaker of the House, to serve at their pleasures. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 7. Amends G.S. 58-248.33(d) so that it will read:

(d) The Facility shall be administered by a Board of Governors. The Board of Governors shall consist of nine members having one vote each from the classifications hereinafter enumerated plus the Commissioner who shall serve ex officio without vote. Each Facility insurance company member serving on the Board shall be represented by a senior officer of the company. Not more than one company in a group under the same ownership or management shall be represented on the Board at the same time. Five members of the Board shall be selected by the member insurers, which members shall be fairly representative of the industry. To insure representative member insurers, one each shall be selected from the following groups: the American Insurance Association (or its successors), the American Mutual Insurance Alliance (or its successors), the National Association of Independent Insurers (or its successors), all other stock insurers not affiliated with the above groups, and all other nonstock insurers not affiliated with the above groups. The Commissioner of Insurance shall appoint four members of the Board who shall be fire and casualty insurance agents licensed in this State and actively engaged in writing motor vehicle insurance in this State. The Commissioner shall select one agent from among a list of two nominees submitted by the Independent Insurance Agents of North Carolina, Inc., and one agent from among a list of two nominees submitted by the Carolinas Association of Professional Insurance Agents. The initial term of office of said Board members shall be two years. Following the completion of initial terms, successors to the members of the original Board of Governors shall be selected to serve three years. All members of the Board of Governors shall serve until their successors are selected and qualified and the Commissioner may fill any vacancy

on the Board from any of the aforementioned classifications until such vacancies are filled in accordance with the provisions of this Article. The Board of Governors, each of its subcommittees, and each special ad hoc committee of the Facility shall also have as nonvoting members three persons who are not employed by or affiliated with any insurance company and who are appointed by the Governor, Lieutenant Governor, and Speaker of the House, to serve at their pleasures. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 8. Amends G.S. 58-25.1 so that it will read:

The Commissioner may also address to any authorized insurer, rating organization, advisory organization, joint underwriting or joint reinsurance organization, or the North Carolina Rate Bureau or Motor Vehicle Reinsurance Facility, or its officers any inquiry in relation to its transactions or condition or any matter connected therewith. Every corporation or person so addressed shall reply in writing to such inquiry promptly and truthfully, and such reply shall be verified, if required by the Commissioner, by such individual, or by such officer or officers of a corporation, as he shall designate. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 9. Provides that the Bureau may make its 1986 rate filing after July 1, 1986.(THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 9.1. Amends G.S. 58-131.37(a) so that it will read:

(a) In order to serve the public interest, rates shall not be excessive, inadequate, or unfairly discriminatory.(THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 10. Repeals G.S. 58-131.37(b) and (c) which now state:

(b) Rates are not excessive if a reasonable degree of price competition exists at the consumer level with respect to the class of business to which they apply. It is presumed that a reasonable degree of price competition exists if there are a number of insurers actively engaged in the class of business and there are rate differentials in that class of business.

(c) If such competition does not exist, rates are excessive if they clearly produce a long-run underwriting profit that is unreasonably high for the class of business.(THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 11. Rewrites G.S. 58-131.37(d) which now reads:

(d) No rate shall be held to be inadequate unless (i) the rate is unreasonably low for the insurance provided and the continued use of the rate endangers the solvency of the insurer, or unless (ii) the rate is unreasonably low for the insurance provided and the use of the rate by the insurer has, or if

continued will have, the effect of destroying competition or creating a monopoly.(THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Sections 12 and 12.1. Rewrite G.S. 58-131.42 which now reads:

<58-131.42. Disapproval of rates; interim use of rates.--(a) If the Commissioner finds after a hearing that a rate is not in compliance with G.S. 58-131.37, he shall issue an order specifying in what respects it so fails, and stating when, following a reasonable period thereafter, the rate shall be deemed no longer effective. the order shall not affect any contract or policy made or issued prior to the expiration of the period set forth in the order.

(b) Whenever a rate of an insurer is held to be unfairly discriminatory or excessive and the rate is deemed no longer effective by order of the Commissioner issued under subsection (a) of this section, the insurer shall have the option to continue to use the rate for the interim period pending judicial review of the order, provided that the insurer shall place in an escrow account approved by the Commissioner the purported unfairly discriminatory or excessive portion of the premium collected during the interim period. The court, upon a final determination, shall order the escrowed funds or any overcharge in the interim rates to be distributed appropriately, except that refunds to policyholders that are de minimis shall not be required.(THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 13. Adds a new subsection G.S. 58-131.61.(THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 14. Adds a new Article 38 "Insurance Regulatory Reform Act." which provides:

- <58-470. A short title.
- <58-471. Legislative findings.
- <58-472. Scope. This Article covers:
 - (4) Fire Insurance
 - (5) Miscellaneous Property Insurance
 - (6) Water Damage Insurance
 - (7) Burglary and Theft Insurance
 - (8) Glass Insurance
 - (9) Boiler and Machinery Insurance
 - (10) Elevator Insurance
 - (11) Animal Insurance
 - (12) Collision Insurance
 - (13) Personal Injury Liability Insurance
 - (14) Property Damage Liability Insurance

- (18) Title Insurance
- (19) Motor Vehicle and Aircraft Insurance
- (20) Marine Insurance
- (21) Marine Protection and Indemnity Insurance
- (22) Miscellaneous Insurance

The Article does not apply to insurance written under the following Articles:

- Article 12B North Carolina Rate Bureau
- Article 18A Essential Property Insurance for Beach Area Property
- Article 18B Fair Access to Insurance Requirements
- Article 25A North Carolina Motor Vehicle Reinsurance Facility
- Article 36 Surplus Lines

The Article also does not apply to the listed types of insurance.

<58-473. Prohibits cancellation of policies except at their expiration or anniversary dates except for the stated reasons. The cancellation is not effective unless the insured is mailed or delivered notice of cancellation with a 15 day notice period.

<58-474. Provides for notice of nonrenewal, premium increases, or changes in coverage shall not be effective until the insured has been mailed or delivered notice of the action with a 45 day notice period.

<58-475. Provides that the insured shall be given 45 days notice when the insurer intends to renew a policy with premium increases or coverage changes. The insured may cancel the policy within 30 days of receiving the notice, paying for the coverage during that period at the old rates and with the old coverages.

<58-476. Provides that if the insurer loses treaty insurance covering a type of insurance it has been selling, the insurer may cancel the insurance after filing with the Commissioner a plan which will inform the Commissioner of the efforts taken to minimize the market disruption of no longer providing that type of insurance.

<58-477. Provides that if an insurer stops any of its business through a North Carolina agency, that insurer shall provide the Commissioner with information.

<58-478. Provides that there is no cause of action for defamation or invasion of privacy for any communication, unless made in bad faith and with malice, relating to cancellation of policies, cessation of business, nonrenewal, or any evidence submitted at any court hearing, administrative hearing, or informal inquiry related to cancellation, nonrenewal, or cessation of business through an agency.

<58-479. Provides that when an insurer terminates by nonrenewals an entire book of business, it must give the

Commissioner 60 days notice and must be under an approved plan to minimize market disruption. The 60 days can be waived if the company's solvency would otherwise be impaired. In-term cancellation of an entire book of business, unless done to prevent impairment of solvency, is to be considered a unfair trade practice making the company subject to sanctions from the Commissioner.

<58-480. (a) Policy forms must be filed with the Commissioner for 90 days before they can be put into effect. Insurers may negotiate and contract with the insured to limit or exclude coverage for punitive damages.

(b) Rates must be filed with the Commissioner for 60 days before they can be put into effect.

(c) A filing that does not contain the statistical and rating information required by subsections (d) and (e) of this section will be returned as incomplete.

(d) The filing shall contain a detailed list of new rates, rules, and policies forms along with those being replaced and a detailed listing of changes made to the above.

(e) The filing shall contain:

- (1) North Carolina earned premiums at actual and current rate level, losses and loss adjustment expenses, all based on paid and incurred bases without trending or other modifications including loss ratios;
- (2) Credibility factor development and application;
- (3) Loss development factor derivation and application;
- (4) Trending factor development and derivation;
- (5) Changes in premium base resulting from rating exposure trends;
- (6) Limiting factor development and derivation;
- (7) Overhead expense development and application;
- (8) Percent rate change;
- (9) Final proposed rates;
- (10) Investment earnings and unearned premium reserves;
- (11) Statistical plans and programs;
- (12) Investment earnings on capital and surplus;
- (13) Capacity;
- (14) Any other information required by any rule adopted by the Commissioner.

(f) Makes it unlawful for an insurer to collect premiums based on rates not approved under this Article or Article 13C.

<58-481. Provides for penalties and restitution for violations of this Article. (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 15. Repeals G.S. 58-131.53(b) which now reads:

(b) Whenever any insurance company cancels its relationship with a North Carolina insurance agency or whenever the relationship between the agency and the company is in any way

terminated, the company shall notify the Commissioner. The notification of the Commissioner shall state the number and kinds of policies written through the agency.

Repeals G.S. 58-131.56 which now reads:

<58-131.56. Policy forms.--Except for fidelity, surety, or guaranty bonds and except as to inland marine risks which by general custom of the business are not written according to manual rates or rating plans, no policy form applying to insurance on risks or operations covered by this Article shall be delivered or issued for delivery unless it has been filed with the Commissioner and either he has approved it, or 90 days have elapsed and he has not disapproved it.

Repeals G.S. 58-131.59 which now reads:

<58-131.59. Notice of coverage or rate change.--Whenever an insurer changes the coverage other than at the request of the insured or changes the premium rate, it shall give the insured written notice of such coverage change or premium rate change at least 15 days in advance of the effective date of such change or changes with a copy of such notice to the agent. This section shall apply to all policies and coverages subject to the provisions of this Article. (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 16. Rewrites the proviso in G.S. 58-131.38(1) which currently reads: provided, however, that countrywide expense and loss experience and other countrywide data shall be considered where credible North Carolina experience or data is not available. (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 17. Requires that G.S. 58-480 and G.S. 58-131.39 should be construed together since they are on the same matter or subject. G.S. 131.39 currently reads:

<131.39. Filing of rates and supporting data.--(a) Except as to inland marine risks which by general custom of the business are not written according to manual rates and rating plans, every admitted insurer and every licensed rating organization, which has been designated by any insurer for the filing of rates under G.S. 58-131.41, shall file with the Commissioner all rates and all changes and amendments thereto made by it for use in this State prior to the time they become effective.

(b) The Commissioner may require the filing of supporting data including:

(1) The experience and judgment of the filer, and to the extent the filer wishes or the Commissioner requires, of other insurers or rating organizations;

(2) The filer's interpretation of any statistical data relied upon; and

(3) Descriptions of the methods employed in setting the rates.

(c) Upon written consent of the insured, stating his reasons therefor, a rate or deductible or both in excess of that provided

by an otherwise applicable filing may be used on a specific risk, provided that it is filed with the Commissioner in accordance with subsection (a) of this section." (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 18. Rewrites the heading and first phrase of G.S. 58-54.4 which now reads:

(11) Certain Business Practices in Connection with First-Party Claims.--In connection with first-party claims, committing or performing with such frequency as to indicate a general business practice any of the following: (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 19. Rewrites G.S. 58-248.33(b)(1)e. which now reads:

e. Any other motor vehicle insurance limits in the amount required by any law or regulatory agency regulation for those motor carriers who furnish proof of insurance or file certificates of insurance with any regulatory agency in order to comply with the security or other financial responsibility requirements of the North Carolina Utilities Commission and the United States Interstate Commerce Commission or who are subject to financial responsibility requirements established under the Federal Motor Carrier Act of 1980. (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 20. Current subdivisions a. and b. of G.S. 58-54.4(7) define as "unfair methods of competition and unfair and deceptive acts or practices in the business of insurance" the discrimination between individuals of the same class and expected life expectancy in life insurance and the discrimination between individuals of essentially the same hazard in accident or health insurance. The new sections prohibit discrimination based on geographic location and the age of the residential property insured. (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 21. G.S. 58-173.2, which is amended by this section, provides definitions for use in Article 18A which deals with "Essential Property Insurance for Beach Area Property." (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 22. Adds language to G.S. 58-173.8(b) which will read, with the addition noted:

(b) If the Association [North Carolina Insurance Underwriting Association] determines that the property is insurable and that there is no unpaid premium due from the applicant for prior insurance on the property, the Association, upon receipt of the premium, or such portion thereof, as is prescribed in the plan of operation, shall cause to be issued a policy of essential property insurance, including the offering of additional extended coverage, or crime insurance, or both, for a

term of one year. Any policy issued pursuant to the provisions of this section shall be renewed annually, upon application therefor, so long as the property meets the definition of 'insurable property' set forth in G.S. 58-173.2(5). (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 23. Rewrites the first sentence of G.S. 58-173.20 which currently reads:

"The association formed pursuant to the provisions of this Article shall have authority on behalf of its members to cause to be issued basic property insurance, including property insurance for farm risks[,] policies, to reinsurance in whole or in part, any such policies, and to cede any such reinsurance." (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 24. Adds a new subsection to G.S. 58-173.17 which rewrote the purpose and geographic coverage of the Article about "Fair Access to Insurance Requirements." (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 25. Adds language to G.S. 58-173.2(5) which provides the definition for "insurable property" to provide that any one or two family dwellings built or any structure commenced after January 1, 1970 built in substantial compliance with either the:

(1) Federal Manufactured Home Construction and Safety Standards, or its successors;

(2) The North Carolina Uniform Residential Building Code; or

(3) The North Carolina Building Code can be insured by the Association under the BEACH PLAN. (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 26. Adds a new Article to Chapter 58 which provides statutory authority for the creation of risk pools by local governments to provide insurance and provides for the oversight by the Commissioner of these pools to insure their solvency.

<58-490. Provides a short title and defines 'local government' as any county or municipal corporation located in this State. Note that the words "municipal corporation" should be replaced with the word "city" since the words "municipal corporation" are not defined in Chapter 160A except to be used in special purpose corporations which are not covered by that Chapter.

<58-491. Provides for pooling of property, liability, and workers' compensation coverage. There already has existed for some time a pooling arrangement for workers' compensation and health insurance among local governments.

<58-492. Provides that each pool shall be run by a board of trustees and provides for the powers and prohibitions applicable to the board of trustees.

<58-493. Provides for the contents of the contract between the participants of the pools.

<58-494. Provides for the termination of any pool.

<58-495. Provides for an audit, at least every three years, by the Department of Insurance of each pool at pool expense.

<58-496. Provides for procedures in the event of the insolvency or financial impairment of the pool.

<58-497. Provides for immunity of administrators and boards of trustees for good faith performance of their powers and duties.

<58-498. Provides that the local government pools are not covered by the guaranty associations or solvency funds provided for in Chapters 58 and 97. (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 27. Adds language to G.S. 153A-435(a) and G.S. 160A-485(a) so that they will read, respectively:

(a) A county may contract to insure itself and any of its officers, agents, or employees against liability for wrongful death or negligent or intentional damage to person or property or against absolute liability for damage to person or property caused by an act or omission of the county or any of its officers, agents, or employees when acting within the scope of their authority and the course of their employment. Participation in a local government risk pool pursuant to Article 39 of General Statute Chapter 58 shall be deemed to be the purchase of insurance for the purposes of this section. The board of commissioners shall determine what liabilities and what officers, agents, and employees shall be covered by any insurance purchased pursuant to this subsection.

(a) Any city is authorized to waive its immunity from civil liability in tort by the act of purchasing liability insurance. Participation in a local government risk pool pursuant to Article 39 of General Statute Chapter 58 shall be deemed to be the purchase of insurance for the purposes of this section. Immunity shall be waived only to the extent that the city is indemnified by the insurance contract from tort liability. No formal action other than the purchase of liability insurance shall be required to waive tort immunity, and no city shall be deemed to have waived its tort immunity by any action other than the purchase of liability insurance. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 28. Provides immunity from suit to the Commissioner, his representatives, any director, administrator, or employee for the creation and operation of a market assistance program. (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 29. Provides for reporting about open claims when a "claims made" policy is not renewed and "extended reporting

period" coverage is offered to the insured under a commercial liability coverage policy. (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 30. Amends G.S. 58-27.22 which provides for the powers and duties of the Public Officers and Employees Liability Insurance Commission. The first sentence of this section will read: "The Commission may acquire from an insurance company or insurance companies a group plan of professional liability insurance covering the law enforcement officers and/or public officers and employees of any political subdivision of the State." This section then adds a new, all inclusive, definition of "political subdivision" to this Article. (THIS SECTION WAS RECOMMENDED BY THIS COMMISSION.)

Section 31. Adds a new subdivision to provide that the Commission on Health Services may adopt the rules described in the section. This section is permissive and does not require the adoption of the rules. (THIS SECTION WAS A MODIFIED RECOMMENDATION OF THIS COMMISSION.)

Section 32. Adds a new subsection to G.S. 58-150. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 33. G.S. 58-248.33(g)(6) is more than a full page long in the General Statutes and this new sentence probably is added after the third paragraph as a fourth paragraph. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 34. Adds a new subsection to G.S. 58-248.34 which has been previously amended by this act. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 35. Rewrites G.S. 55-19(a) which now reads: "(a) Except as indemnification of a director or officer of a corporation is permitted by this section or by G.S. 55-20 [Indemnification in actions by outsiders] and 55-21 [Indemnity for litigation expenses in corporate action], no provision, hereafter made or adopted, whether contained in the charter, the bylaws, a resolution, a contract or otherwise, whereby the corporation purports to exempt or indemnify any director or officer of a corporation with respect to any liability or litigation expenses arising out of his activities as a director or officer shall be valid." (THIS SECTION WAS A MODIFIED RECOMMENDATION OF THIS COMMISSION.)

Section 36. Rewrites G.S. 55-19(b) which now reads: "(b) As used in this section and in G.S. 55-20 and 55-21, the term 'officer' includes any dominant shareholder engaged to perform services for the corporation, whether as employee or independent contractor; and the term 'person' includes the legal

representative of such person." (THIS SECTION WAS A MODIFIED RECOMMENDATION OF THIS COMMISSION.)

Section 37. Adds words to G.S. 55-19(c) so that it will read:

"(c) Anything in this section or in G.S. 55-20 or 55-21 to the contrary notwithstanding, a corporation shall have power to purchase and maintain insurance on behalf of any person who is or was a director, officer, employee or agent of the corporation, or is or was serving at the request of the corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, trust or other enterprise or as a trustee or administrator under an employee benefit plan against any liability asserted against him and incurred by him in any such capacity, or arising out of his status as such, whether or not the corporation would have the power to indemnify him against such liability."

(THIS SECTION WAS A MODIFIED RECOMMENDATION OF THIS COMMISSION.)

Section 38. Adds words to G.S. 55-19(d) so that it will read:

"(d) Expenses incurred by a director, officer, employee or agent in defending a civil or criminal action, suit or proceeding may be paid by the corporation in advance of the final disposition of such action, suit or proceeding as authorized by the board of directors in the specific case or as authorized or required under any charter or bylaw provision or by any applicable resolution or contract upon receipt of an undertaking by or on behalf of the director, officer, employee or agent to repay such amount unless it shall ultimately be determined that he is entitled to be indemnified by the corporation against such expenses." (THIS SECTION WAS A MODIFIED RECOMMENDATION OF THIS COMMISSION.)

Section 39. Adds words to G.S. 55-20(a) so that it will read:

(a) When by reason of the fact that he is or was serving as director, officer, employee or agent of a corporation, or in any such capacity at the request of the corporation in any other corporation, partnership, joint venture, trust or other enterprise, any person is or was a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceedings, whether civil, criminal, administrative or investigative, not brought by the corporation nor brought by any party seeking derivatively to enforce a liability of such a person to the corporation, such person shall be entitled to indemnification or reimbursement by the corporation for any expenses including attorneys' fees, or any liabilities which he may have incurred in consequence of such action, suit or proceeding, under the following conditions:

(1) If such person is wholly successful in his defense, or if the proceeding is an administrative or investigative proceeding which does not result in the indictment, fine or

penalty of such person, he shall be entitled to reimbursement from the corporation of all his reasonable expenses of defense or participation, including attorneys' fees, or

(2) If such person is not wholly successful or is unsuccessful in his defense, or the proceeding to which he is a party results in his indictment, fine, or penalty, the corporation shall pay such expenses of defense or participation, including attorneys' fees, and the amount of any judgment, money decree, fine, penalty, or settlement for which he may have become liable, if: " (THIS SECTION WAS A MODIFIED RECOMMENDATION OF THIS COMMISSION.)

Section 40. Changes words in G.S. 55-21(c) so that it will read:

(c) Whenever indemnification or reimbursement as provided in this section is sought, the court may in its discretion order notice of the claim thereof to be sent to the shareholders in such manner and in such form as it may approve, at the expense of the corporation. All shareholders so notified may be heard in opposition to the relief requested." (THIS SECTION WAS A MODIFIED RECOMMENDATION OF THIS COMMISSION.)

Section 41. Amends the first paragraph of G.S. 20-279.21(b)(3) so that it will read:

(3) No policy of bodily injury liability insurance, covering liability arising out of the ownership, maintenance, or use of any motor vehicle, shall be delivered or issued for delivery in this State with respect to any motor vehicle registered or principally garaged in this State unless coverage is provided therein or supplemental thereto, in limits for bodily injury or death set forth in subsection (c) of G.S. 20-279.5, under provisions filed with and approved by the Commissioner of Insurance, for the protection of persons insured thereunder who are legally entitled to recover damages from owners or operators of uninsured motor vehicles and hit-and-run motor vehicles because of bodily injury, sickness or disease, including death, resulting therefrom; and (provided-that-an-insured-shall-be-entitled-to-secure-increased-limits-coverage-of-twenty-five-thousand-dollars-(\$25,000)-because-of-bodily-injury-to-or-death-of-one-person-in-any-one-accident-and,-subject-to-said-limit-for-one-person,-fifty-thousand-dollars-(\$50,000)-because-of-bodily-injury-to-or-death-of-two-or-more-persons-in-any-one-accident-if-the-policy-of-such-insured-carries-liability-limits-of-equal-or-greater-amount-for-the-protection-of-third-persons) provided, an insured is entitled to secure additional coverage up to the limits of bodily injury liability in the owner's policy of liability insurance that he carries for the protection of third persons. Such provisions shall include coverage for the protection of persons insured thereunder who are legally entitled to recover damages from owners or operators of uninsured motor vehicles because of injury to or destruction of the property of such insured, with a limit in the aggregate for

all insureds in any one accident of (~~ten-thousand-dollars~~
+\$10,000) up to the limits of property damage liability in the owner's policy of liability insurance, and subject, for each insured, to an exclusion of the first one hundred dollars (\$100.00) of such damages. Such provision shall further provide that a written statement by the liability insurer, whose name appears on the certification of financial responsibility made by the owner of any vehicle involved in an accident with the insured, that such other motor vehicle was not covered by insurance at the time of the accident with the insured shall operate as a prima facie presumption that the operator of such other motor vehicle was uninsured at the time of the accident with the insured for the purposes of recovery under this provision of the insured's liability insurance policy. The coverage required under this subdivision shall not be applicable where any insured named in the policy shall reject the coverage. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 42. Adds new language to subdivisions (b)(3) and (b)(4) of G.S. 20-279.21. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 43. Amends G.S. 58-248.33(b)(2) so that it will read:

(2) Additional ceding privileges for motor vehicle insurance shall be provided by the Board of Governors if there is a substantial public demand for a coverage or coverage limit of any component of motor vehicle insurance up to the following:

Bodily injury liability: one hundred thousand dollars (\$100,000) each person, three hundred thousand dollars (\$300,000) each accident;

Property damage liability: fifty thousand dollars (\$50,000) each accident;

Medical payments: two thousand dollars (\$2,000) each person;

Underinsured motorist: one hundred thousand dollars (\$100,000) each person and three hundred thousand dollars (\$300,000) each accident for bodily injury liability;

Uninsured motorist: one hundred thousand dollars (\$100,000) each person and each accident for bodily injury and ten thousand dollars (\$10,000) for property damage (one hundred dollars (\$100.00) deductible). (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 44. G.S. 58-44.8 is amended so that it will read: No licensed agent of any insurer shall solicit anywhere in the boundaries of the State of North Carolina, or receive or transmit an application or premium of insurance for a company not authorized to do business in the State, except as provided in ~~G.S. 58-53.1~~ Article 36 of this Chapter. (THIS SECTION WAS NOT

A RECOMMENDATION OF THIS COMMISSION.)

Section 45. G.S. 58-422(8) is amended so that it will read:

(8) "Surplus lines insurance" means any insurance in this State of risks resident, located, or to be performed in this State, permitted to be placed through a surplus lines licensee with a nonadmitted insurer eligible to accept such insurance, other than reinsurance, wet marine and transportation insurance, insurance independently procured, life and accident or health insurance, and annuities. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 46. G.S. 58-424(a)(2)c. is amended so that it will read:

c. In the case of an "insurance exchange" created by the laws of individual states, maintain capital and surplus, or the substantial equivalent thereof, of not less than fifteen million dollars (\$15,000,000) in the aggregate. For insurance exchanges which maintain funds for the protection of all insurance exchange policyholders, each individual syndicate shall maintain minimum capital and surplus, or the substantial equivalent thereof, of not less than (four) one million five hundred thousand dollars (\$4,150,000). In the event the insurance exchange does not maintain funds for the protection of all insurance exchange policyholders, each individual syndicate shall meet the minimum capital and surplus requirements of subdivision (2)a. of this section. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 47. The first sentence of G.S. 58-131.44 is amended so that it will read:

(a) No advisory organization shall conduct its operations in the State unless and until it has obtained a license from and filed with Commissioner:. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 48. The first sentence of G.S. 58-131.45 is amended so that it will read:

(a) Every group, association, or other organization of insurers which engages in joint underwriting or joint reinsurance through such group, association, or organization, or by standing agreement among the members thereof, shall obtain a license from and file with the Commissioner:. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 49. Apparently intends to amend the third sentence of G.S. 57B-3(a) so that it will read:

A foreign corporation may qualify under this Chapter, subject to its (registration-to-do-business-in-this-State-as-a-foreign

~~operation under Article 17 of Chapter 58~~) full compliance with Article 17 of Chapter 58. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 50. Adds a provision to G.S. 20-130.1 to allow the State Fire Marshal to operate a red light on his vehicle. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 51. Allows the Manufactured Housing Board to impose a five hundred dollar (\$500.00) penalty on any person violating the provisions of Part 1 of Article 9A of Chapter 143 of the General Statutes. (THIS SECTION MODIFIED A RECOMMENDATION OF THIS COMMISSION.)

Section 52. Amends G.S. 58-16.3 so that it will read:
The provisions of G.S. 58-16, (58-16.1), 58-16.2, 58-17, 58-18, 58-21, 58-22, 58-25, 58-25.1, 58-27, and 58-63 apply to employers that furnish proof of financial responsibility to the Commissioner under G.S. 97-93(a)(2) and to persons that administer workers' compensation self-insurance for such employers. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 53. G.S. 58-151 is amended by redesignating the existing section as subsection (a) and adding the language contained in the act. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 54. Amends G.S. 97-94(a) so that it will read:
(a) Every employer subject to the compensation provisions of this Article shall, within 30 days, after this Article takes effect, file with the (Commissioner of Insurance) Industrial Commission, in form prescribed by it, and thereafter, annually or as often as may be necessary, evidence of his compliance with the provisions of G.S. 97-93 and all others relating thereto. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 55. Incorporates the Federal Rule of Civil Procedure 11 into the North Carolina Rules of Civil Procedure in an effort to curb frivolous lawsuits. (THIS SECTION MODIFIED A RECOMMENDATION OF THIS COMMISSION.)

Section 56. Provides that in negligence actions and in all lawsuits where there is a claim for punitive damages, and where the amount in controversy exceeds \$10,000, the pleading shall state that the amount sought is in excess of \$10,000 with the exact amount to be provided in a written statement upon request after the filing of the claim. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 57. A severability section. (THIS SECTION WAS NOT A RECOMMENDATION OF THIS COMMISSION.)

Section 58. Effective date section. (THIS SECTION MODIFIED A RECOMMENDATION OF THIS COMMISSION.)

The Committee Substitute for SB 868 passed by the Senate Judiciary Committee I contained modifications of several of the recommendations of this Commission.

It recommended that there be no limitation on punitive damages but that punitive damages in excess of \$500,000 be paid to the clerk of the court and ultimately be placed in the State's General Fund.

It recommended that there be a \$500,000 cap on pain and suffering.

It recommended that the jury itemize verdicts so that the cap could be applied.

It recommended a Political Subdivision Tort Claims Act with a maximum exposure to political subdivisions of \$500,000 per occurrence and allowed the political subdivisions to settle in any amount up to that limitation without Court supervision.

Neither the Committee Substitute for SB 868 passed by the Senate Judiciary Committee I nor Chapter 1027 of the 1985 Session Laws addressed the concepts of the joint and several liability, collateral source rule, structured settlements, or making workers' compensation the sole remedy for actions against design professionals.

APPENDIX J

January 7, 1987

M E M O R A N D U M

FROM: KENNETH T. LEVENBOOK, COMMISSION COUNSEL
SUBJECT: TORT REFORM STATUTES OF OTHER STATES
TO: COMMISSION MEMBERS

At the last meeting I was instructed by the Commission to survey the other states and obtain copies of the statutes passed or considered by those states with regard to various tort reforms and to actions taken by those states to assist nonprofit corporations in protecting officers and directors from lawsuits.

After the meeting, I sent a letter to each state requesting copies of the relevant statutes. I have received responses from 21 states. I have read and studied the statutes that were sent to me and the following comments are a distillation of the provisions that were either passed by those states or that are still under consideration pursuant to their legislative rules.

Copies of all statutes mentioned in this memorandum are available from me upon request.

ALABAMA

H. 213 was this state's attempt to address the liability crisis and tort reforms. The official Synopsis attached to the bill indicates that the Alabama Medical Liability Act of 1986 provides for periodic payments of awards in excess of \$100,000 if requested by any party, provides that awards for noneconomic damages shall not exceed \$250,000, allows the introduction of evidence concerning collateral sources, limits medical malpractice actions to \$1,000,000, and provides a limitation on contingency fees in medical malpractice actions and limits the fee that may be collected by the defense attorney to equal to that collected by the plaintiff's attorney.

ALASKA

The Conference Committee Substitute of Senate Bill No. 377:
**provides for a \$500,000 cap on noneconomic damages (but this cap does not apply to disfigurement or severe physical impairment);

**provides that punitive damages shall not be awarded in the absence of "clear and convincing evidence;"

**provides for periodic payment of damages;

**provides that, except for the results of gross negligence, no recovery may be made from directors and officers of nonprofit

corporations, public or nonprofit hospitals, local school boards, citizen's advisory committees of municipalities;

**provides that the defendant in a tort action may introduce evidence concerning collateral sources of compensation to the plaintiff;

**provides that no defendant may be liable for more than twice his proportionate share of damages; and

**provides that after an offer is made for settlement of the case, if the plaintiff does not obtain more than the amount offered, the interest payable on the award shall be reduced.

AZARONA

The General Assembly passed, but the Governor vetoed legislation calling for structured settlements, limitations on joint and several liability, collateral source rule modification, and scheduled contingent attorneys' fees.

Two propositions, to cap damages and limit attorneys' fees were scheduled for vote.

CALIFORNIA

In this state, Proposition 51, which was approved by the voters at the June 3, 1986 statewide primary election, changed the rules governing who must pay for noneconomic damages by limiting the liability of each responsible party in a lawsuit to that portion of the noneconomic damages that is equal to the responsible party's share of fault. The courts still can require one person to pay the full cost of economic damages, if the other responsible parties are not able to pay their share.

COLORADO

Senate Bill No. 67 concerned damages awards in civil actions and contains 3 substantive sections.

**Section 1 provides for a \$250,000 cap on awards for noneconomic damages, which means damages suffered by the "person suffering the direct or primary loss or injury," "unless the court finds justification by clear and convincing evidence" for allowing more. In cases of awards for derivative noneconomic loss or injury to persons other than the person suffering the direct or primary loss or injury, the court is required to find the clear and convincing evidence for any award of damages and is not granted the discretion of increasing the award to more than \$250,000.

**Section 2 provides for special requirements in actions against architects, engineers, and land surveyors.

**Section 3 provides for the application of the collateral source rule in civil actions.

Senate Bill No. 70 concerns joint and several liability in civil actions.

House Bill No. 1197 concerns the award of damages, provides for limitations and distribution of those awards. This statute limits exemplary damages (punitive damages) to an amount equal to

the award of actual damages. The court may reduce or disallow punitive damages when it deems appropriate or may raise the damages to three times the actual damages under certain circumstances. One-third of all punitive damages shall be paid into the State General Fund with the other two-thirds going to the prevailing party.

CONNECTICUT

Public Act 86-338:

**limits attorneys' fees (Section 1);
**requires periodic payments for awards in excess of \$200,000 (Section 2);

**eliminates joint and several liability for noneconomic and economic damages in negligence actions for personal injury and wrongful death, and provides for apportioning among the remaining defendants of any uncollectable portion of the judgment (Section 3);

**adds the collateral source rule and requires the reduction of the award by the judge (Section 4);

**allows any party to request that the judge make a ruling that any portion of the lawsuit was frivolous, which can be used in a further action for the recovery of costs and attorneys' fees (Section 8); and

**provides immunity for any person serving on the board of a nonprofit corporation unless the damage or injury was caused by the wilful or wanton actions of the person (Section 10).

FLORIDA

During the 1986 Session Florida's legislature passed Chapter 86-160, the Tort Reform and Insurance Act of 1986 which contains 70 sections. The first 49 deal with insurance regulation, including rate regulation, and with permitting professions to pool their insurance needs, and with providing medical malpractice insurance.

Section 50 provides that any tort reforms will apply to all actions in tort and contract which arise on or after July 1, 1986.

Section 51 provides that there must be a reasonable showing on the record or by the claimant which would provide a reasonable basis for recovery of punitive damages.

Section 52 provides that, except in the case of class action suits, the judgment for punitive damages shall not exceed three times the amount of compensatory damages awarded to each person by the trier of fact. That the jury shall not be instructed about this limitation but that the judge shall reduce the amount of the award in accordance with this provision. 40% of all punitive damages shall be paid to the claimant. The remaining 60% shall be paid to the Public Medical Assistance Trust Fund if the action was for personal injury or wrongful death or to the General Revenue Fund in all other cases. Attorneys' fees, under a

contingency fee agreement, shall be based only on the 40% received by the claimant.

Section 54 provides for a settlement conference at the discretion of the presiding judge to be held at least 3 weeks before the date set for trial and attended by the attorneys who will conduct the trial and persons with authority to settle the case.

HAWAII

Hawaii passed S.B. No. S1-86 which was entitled "A BILL FOR AN ACT RELATING TO LIABILITY."

This act contained tort reforms that requires the court's approval of attorneys' fees for both the plaintiff and defendant in tort actions, changes the standard for the award of attorneys' fees in frivolous lawsuits from "completely frivolous" to "frivolous," provides for periodic payments of damages in cases against the State and counties where the amount awarded exceeds \$1,000,000, provides for the collateral source rule, abolishes joint and several liability, provides for a \$375,000 limitation on damages awarded for pain and suffering, and provides for a "court annexed arbitration program within the judiciary" to deal with cases having a probable jury award, exclusive of interest and costs of \$150,000 or less.

ILLINOIS

On the last day of the 1986 session, the Illinois legislature passed SB 1200, which is 141 pages long and, in part:

**incorporates Rule 11a of the federal rules of civil procedure into the Illinois law to provide sanctions for the filing of frivolous pleadings and lawsuits (Article 2);

**provides that pleading shall not contain any prayer for punitive damages, which may be added later, and permits the court to lower a punitive damages award it finds excessive (Article 3);

**except in cases of environmental damage or medical malpractice, eliminates joint and several liability for any defendant found to be less than 25% responsible for the damages suffered by the plaintiff (Article 5);

**provides for the reduction of an award by the amount paid to the plaintiff from other sources when that amount is \$25,000 or more; and

**grants immunity from suit to officers and directors of nonprofit corporations serving without compensation unless the act or omission involved wilful or wanton conduct (Article 7).

MARYLAND

Senate Bill No. 558:

**provides for a \$350,000 limitation of awards for noneconomic damages; and

**provides for periodic payments and structured awards for future economic damages.

MINNESOTA

H.F. No. 1950 sought to prohibit the allegation of punitive damages in the complaint until after discovery was complete in an action.

MISSOURI

SB 663:

**caps awards for noneconomic damages in medical malpractice actions at \$350,000 (Section 5);

**in medical malpractice actions requires a showing of wilful, wanton, or malicious misconduct before punitive damages may be awarded (Section 5.5);

**provides for periodic payment of damages for future losses in medical malpractice actions at the request of any party (Section 7); and

**eliminates joint and several liability in medical malpractice actions.

NEW HAMPSHIRE

Chapter 227 (HB 513) of the New Hampshire Laws, 1986 is an act relative to tort reform and insurance. It, in part:

**provides for the award of attorneys' fees against a party raising a frivolous action or defense;

**outlaws all punitive damages unless they are specifically authorized by law;

**limits municipal liability for tort actions to \$150,000;

**places a cap on noneconomic damages at \$875,000; and

**requires the filing with the court of all written contingency fee agreements at the time the original pleadings are filed.

NEW JERSEY

Several bills are under consideration by the General Assembly and are in various stages of the legislative process. AB 2400 through AB 2403 contain proposed tort reforms. They have, as of last report, passed the Assembly and are pending in the Senate.

AB 2400

**sets several caps on noneconomic damages based on the severity of the injuries:

minor injuries without permanent disability	\$5,000
catastrophic injuries	\$300,000
all other injuries	\$100,000;

**eliminates awards for noneconomic damages against public entities and public employees unless the actual medical treatment expenses exceed \$1,000;

**provides for the collateral source rule in actions against public entities or public employees;

**provides for immunity from lawsuit for persons serving without compensation on nonprofit corporation boards "unless the actions evidence a reckless disregard for the duties imposed by the position;"

**provides for immunity from lawsuit for persons serving as volunteers on municipal or governmental bodies "unless the actions evidence intentional wrongdoing;"

**provides for immunity from lawsuit for persons serving as volunteer sports coach, manager, or official unless the injuries are the result of wilful, wanton, or grossly negligent actions.

AB 2401:

**provides for deductions for payments from collateral sources in all personal injury lawsuits except those arising out of automobile accidents;

**rewrites the product liability laws;

**provides that punitive damages shall be awarded only "where there has been a showing, beyond a reasonable doubt, that a tortfeasor knowingly acted in flagrant disregard of the injured party's legal rights," only when there is an award of economic damages to the plaintiff, punitive damages may not be awarded when the tortfeasor's actions complied with the applicable governmental regulations, 5% of all punitive damages shall be paid into the Public Entities Liability Reparation Fund to help defray claims of over \$500,000 against public entities;

**eliminates joint and several liability for contribution by a joint tortfeasor who is a public employee acting within the scope of his employment; and

**modifies New Jersey's worker's compensation law.

AB 2402:

**provides for structured settlements for all awards in excess of \$200,000.

AB 2403:

**requires arbitration of claims where the court determines that the amount in controversy is \$20,000 or less.

NEW YORK

Chapters 220 and 221 which related to liability insurance reform provide immunity from liability, except for the results of gross negligence, for directors and officers of volunteer and charitable groups, and to allow these organizations to purchase group property/casualty insurance.

OHIO

The Ohio General Assembly's 116th Session considered a Conference Committee Report containing 124 pages which proposed, among other things, deducting benefits and/or payments from collateral sources from awards; permitting structured settlements when awards exceed \$100,000; modifying joint and several liability; authorizing hearings to determine when lawsuits are frivolous; and authorizing pre-trial settlement offers which would require nonjudicial settlement when an offer exceeds the plaintiff's demand.

OKLAHOMA

SB 488 which was signed into law by the Governor of Oklahoma on June 24, 1986 provides the following tort reforms:

**punitive damages, when based on wanton and reckless disregard of the rights of another based on clear and convincing evidence, shall not exceed the amount of actual damages awarded to the plaintiff unless that jury wants to give punitive damages for the sake of example, under which circumstances the limitation does not apply (Section 1); and

**in frivolous suits, the prevailing party may receive an award of up to \$10,000 to cover attorneys' fees and costs (Section 3).

WASHINGTON

Engrossed Substitute Senate Bill No. 4630 as amended by the House was enacted with the intent to reduce costs associated with the tort system, while assuring that adequate and appropriate compensation for persons injured through the fault of others is available. It provides, in part:

**for court review, upon petition by a named party in any tort action, to determine the reasonableness of that party's attorneys' fees (Part II);

**limits damages for noneconomic damages to 43% of the average annual wage of the plaintiff multiplied by the expected life expectancy of the plaintiff (Part III);

**eliminates joint and several liability, making each defendant responsible for his proportionate share of the damages (Part IV);

**provides for periodic payments of damages for future economic losses when the award exceeds \$100,000 (Part VIII); and

**provides for immunity from civil suit for any officer or member of the board of directors of a nonprofit corporation, any superintendent or member of the board of a local school district, or any member of the board of directors of a public or private hospital except in the case of gross negligence.

WEST VIRGINIA

Enrolled H.B. 149, which became effective May 22, 1986 amended the provisions of S.B. 714, which became effective March 3, 1986, and provided, in part, for the following tort reforms:

**in medical malpractice actions, limited awards for noneconomic damages to \$1,000,000; and

**eliminated joint and several liability for defendants found to be 25% or less responsible for the injuries suffered by the plaintiff.

WISCONSIN

1985 Wisconsin Act 340, which relates only to medical malpractice actions, was signed into law on June 12, 1986, and, in part:

**limits total recovery for noneconomic damages, for any single occurrence of medical malpractice, to \$1,000,000 for claims filed in court during the period from June 14, 1986 to December 31, 1990;

**limits attorneys' contingency fees on a sliding scale, including a limit of 1/3 of the first \$1,000,000 (unless the defendant stipulates liability in which case the limit is 1/4 of the first \$1,000,000); and

**requires periodic payments, not to exceed \$500,000 per year to any claimant from the Wisconsin Health Care Liability Insurance Plan and the Patient Compensation Fund (both were established in 1975).

WYOMING

Chapter 100 of the Wyoming Statutes (Enrolled Act No. 45 of the 1986 Budget Session) signed by the Governor into law on March 14, 1986 limits the liability of members of the board of any nonprofit corporation to the results of intentional torts or illegal acts.

APPENDIX K

A BILL TO BE ENTITLED
AN ACT TO LIMIT THE AMOUNT OF DAMAGES FOR NONECONOMIC LOSSES IN
CIVIL CASES TO \$250,000 AND TO PROVIDE FOR ITEMIZED VERDICTS.

The General Assembly of North Carolina enacts:

Section 1. Rule 54. Judgments. of G.S. 1A-1 is amended by adding a new subsection to read:

"(al) No judgment shall be rendered that allows a plaintiff in any civil action to recover damages for noneconomic losses to compensate for pain and suffering, inconvenience, physical impairment, mental anguish, loss of capacity for enjoyment of life, and other nonpecuniary damages that cannot be proven to have a specific economic value, in an amount that exceeds two hundred-fifty thousand dollars (\$250,000). Juries shall not be instructed about the contents of this section."

Sec. 2. Rule 49. Verdicts. of G.S. 1A-1 is amended by adding a new subsection to read:

"(e) In any civil action in which the trier of fact determines that liability exists on the part of the defendant, the trier of fact shall, as a part of the verdict, itemize the amounts to be awarded to the claimant into the following categories of damages:

- (1) Amounts intended to compensate the claimant for economic losses;
- (2) Amounts intended to compensate the claimant for noneconomic losses; and
- (3) Amounts awarded to the claimant for punitive damages, if applicable."

Sec. 3. This act shall become effective October 1, 1987 and shall apply to actions filed on or after that date.

A BILL TO BE ENTITLED
AN ACT TO CREATE A POLITICAL SUBDIVISION TORT CLAIMS ACT.

The General Assembly of North Carolina enacts:

Section 1. Chapter 160A of the General Statutes is amended by adding a new Article to read:

"ARTICLE 26
"POLITICAL SUBDIVISION TORT CLAIMS ACT

"<160A-590. Short Title.--This Article may be referred to as the Political Subdivision Tort Claims Act.

"<160A-591. Definitions.--Unless the context requires otherwise, the following terms shall have the meanings indicated:

- (1) 'Employee' means any employee, officer, involuntary servant, or agent or any former employee, officer, involuntary servant, or agent, or any member of a volunteer fire department or rescue squad, or any other person while acting within the scope of his employment for any political subdivision, whether paid or voluntary.
- (2) 'Political subdivision' shall include any county, city, town, incorporated village, sanitary district, metropolitan water district, county water and sewer district, water and sewer authority, hospital authority, parking authority, special airport district, and airport authority, and all other bodies or agencies regulated by Chapters 153A, 160A, and 160B of the General Statutes.
- (3) 'Scope of employment' means scope of office, employment, service, agency or authority.
- (4) 'Tort' means any action for damages for personal injuries or property damage arising out of the negligence, but not the gross negligence or intentional act, of any political subdivision or of any employee of a political subdivision.

"<160A-592. Claims.--(a) All claims against any political subdivision or against any employee for personal or property damages arising out of an act of negligence shall be filed in the Superior Court of the County in which the political subdivision is located. As a condition precedent to the filing of an action against the political subdivision or employee, the claimant shall give notice to the governing body of the political subdivision against whom the claim is being filed within 180 days of the event out of which the claim arose.

(b) The Court, without jury, shall try all actions filed pursuant to this Article, unless a jury trial is requested by either party.

(c) The trier of fact shall determine whether or not the employee whose alleged negligence gave rise to the claim was acting in the scope and course of his employment as an employee or officer of the political subdivision. If the Court determines that the employee was acting within the scope of his employment, then the employee shall be entitled to be reimbursed by the political subdivision and to be defended by the political subdivision in accordance with the provisions of G.S. 160A-167.

(d) If the Court finds that there was negligence on the part of the employee of the political subdivision while acting within the scope of his employment under circumstances where the political subdivision, if a private person, would be liable to the claimant in accordance with the laws of North Carolina, and that those circumstances were the proximate cause of the injury claimed, and that there was no contributory negligence on the part of the claimant or the person in whose behalf the claim is asserted, the Court shall determine the amount of damages which the claimant is entitled to be paid and shall issue a judgment directing the payment of the damages by the political subdivision, but in no event shall the amount of damages awarded exceed the sum of one hundred thousand dollars (\$100,000) cumulatively to all claimants on account of injury and damage to any one person unless the political subdivision has purchased liability insurance in excess of one hundred thousand dollars (\$100,000) pursuant to G.S. 153A-435(a) or G.S. 160A-485(a) or any other statute authorizing the purchase of liability insurance and then the damages may be equal to the amount of insurance coverage purchased for the particular harm.

"<160A-593. Appeal to Court of Appeals to act as supersedeas.--The appeal from the decision of the Superior Court to the Court of Appeals shall act as a supersedeas and the political subdivision shall not be required to make payment of any judgment until the questions at issue shall have been finally determined.

"<160A-594. Settlement of Claims.--(a) The governing bodies of political subdivisions covered by this Article may settle, on a case by case basis, any claims, except the claims of minors, in an amount of twenty-five thousand dollars (\$25,000) or less without an action being filed in Superior Court. The political subdivision may make settlements by agreement for claims in excess of twenty-five thousand dollars (\$25,000) and claims of minors or persons non sui juris, provided that these settlements have been reviewed and approved by the Court.

"<160A-595. Limitations on claims.--(a) All claims against political subdivisions arising out of alleged tortious acts shall be barred unless an action is filed in Superior Court within two years after the event out of which the claim arose.

(b) No claims or actions shall arise out of the following 'governmental' functions when exercised directly by the political

subdivisions. Claims and actions may arise when the the following 'governmental' functions are exercised by contractors or subcontractors of political subdivisions.

- (1) making and enforcing ordinances;
- (2) preventing crime and operation of a police force;
- (3) preserving the public health;
- (4) fire prevention, suppression, and operation of a paid or voluntary fire department;
- (5) providing services to the poor;
- (6) educational services;
- (7) animal control;
- (8) control and regulation of bus companies;
- (9) discharge of public employees;
- (10) maintenance of airports;
- (11) operation and maintenance of libraries;
- (12) installation and maintenance of traffic signal lights;
- (13) installation and maintenance of systems providing electricity for street lighting;
- (14) operation and maintenance of parks (where non-city income for their operation and maintenance is incidental);
- (15) garbage disposal (where the service is operated on a nonprofit basis);
- (16) any duties imposed on a political subdivision by statute; and
- (17) any other actions or functions in exercise of police power, or judicial, discretionary, or legislative authority, conferred by their charters or by statute, and when discharging a duty imposed solely for the public benefit.

(c) Notwithstanding any other provision of law, a political subdivision shall be immune from punitive damages.

"<160A-596. Contributory negligence a matter of defense; burden of proof.--Contributory negligence on the part of the claimant or the person in whose behalf the claim is asserted shall be deemed to be a matter of defense on the part of the political subdivision against which the claim is asserted, and that political subdivision shall have the burden of proving that the claimant or the person in whose behalf the claim is asserted was guilty of contributory negligence."

Sec. 2. The first sentence of the second paragraph of G.S. 153A-435(a) is amended by adding immediately after the words "to the extent of insurance coverage" the words "in excess of one hundred thousand dollars (\$100,000)".

Sec. 3. The first sentence of G.S. 160A-485(a) is rewritten to read: "Any city is authorized to waive its immunity from civil liability in tort to the extent it purchases liability insurance

in an amount that exceeds one hundred thousand dollars (\$100,000)."

Sec. 4. G.S. 160A-167 is amended by adding a new subsection to read:

"(c1) Subsection (b) shall not authorize any city, authority, or county to pay all or part of a claim made or civil judgment for punitive damages."

Sec. 5. All local laws and local acts in conflict with this Act are repealed.

Sec. 6. This act shall become effective October 1, 1987 and shall apply to all claims arising on or after that date.

A BILL TO BE ENTITLED
AN ACT TO MODIFY JOINT AND SEVERAL LIABILITY SO THAT A DEFENDANT
IS LIABLE TO A PLAINTIFF ONLY TO THE DEGREE HE WAS RESPONSIBLE FOR
THE DAMAGES SUFFERED BY THE PLAINTIFF.

The General Assembly of North Carolina enacts:

Section 1. Chapter 1B of the General Statutes is amended by adding a new Article to read:

"Article 4.
"Joint Liability.

"1B-9. Abolition of joint and several liability; exceptions.--Joint and several liability for joint tort-feasors is abolished for noneconomic damages and for recovery of economic damages against those tort-feasors whose individual degree of negligence is found to be twenty-five percent (25%) or less under G.S. 1B-10. Joint and several liability shall apply only to economic damages and to tort-feasors whose degrees of negligence are more than twenty-five percent (25%). This section is not intended to modify or in any way affect the doctrine of contributory negligence found in G.S. 1-139 and G.S. 1A-Rule 8. When the trier of fact is a jury, it shall not be instructed on the provisions of this section.

"1B-10. Itemized verdicts.--(a) A trial court upon its own motion may, and when requested by any party shall, direct the jury to find separate special verdicts determining the total amount of damages sustained, the amount of economic and noneconomic damages sustained, and the percentage or proportion of fault attributable to each defendant.

(b) In a matter tried to the Court alone, upon motion of any party, the Court shall determine the total amount of the damages sustained, the economic and noneconomic damages sustained, and the percentage or proportion of fault attributable to each defendant.

"1B-11. Parties.--A plaintiff or any defendant may join as parties any persons who may have caused or contributed to the injury or damage for which the recovery is sought, for the purpose of having determined their respective proportions of fault.

"1B-12. Releases.--A release given to one or more defendants by a plaintiff does not discharge any other defendant unless the release provides for that discharge.

"1B-13. Effect of this Article.--Nothing in this Article affects or impairs any common law or statutory immunity from liability or impairs any right to indemnity or contribution arising from statute, contract, or agreement."

Sec. 2. Articles 1 and 2 of Chapter 1B of the General Statutes shall apply to all actions filed before October 1, 1987.

Sec. 3. This act shall become effective October 1, 1987.

A BILL TO BE ENTITLED
AN ACT TO REGULATE THE AWARD OF PUNITIVE DAMAGES IN CIVIL CASES
AND TO PROVIDE FOR ITEMIZED VERDICTS.

The General Assembly of North Carolina enacts:

Section 1. Rule 54. Judgments. of G.S. 1A-1 is amended by adding a new subsection to read:

"(a1) All judgments providing for the payment of punitive damages shall provide that:

(1) Forty percent (40%) of the award shall be payable to the claimant; and

(2) Sixty percent (60%) of the award shall be payable to the General Fund.

Sec. 2. Rule 49. Verdicts. of G.S. 1A-1 is amended by adding a new subsection to read:

"(f) In any civil action in which the trier of fact determines that liability exists on the part of the defendant, the trier of fact shall, as a part of the verdict, itemize the amounts to be awarded to the claimant into the following categories of damages:

(1) Amounts intended to compensate the claimant for actual losses; and

(2) Amounts awarded to the claimant for punitive damages, if applicable."

Sec. 3. This act shall become effective October 1, 1987 and shall apply to actions filed on or after that date.

A BILL TO BE ENTITLED
AN ACT TO MODIFY THE COLLATERAL SOURCE RULE.

The General Assembly of North Carolina enacts:

Section 1. Rule 43. Evidence. of G.S. 1A-1 is amended by adding a new subsection to read:

"(f) In any action for damages for personal injury or wrongful death, whether in tort or contract, in which liability is admitted or to be determined by the trier of fact and damages are to be awarded to compensate a party for losses sustained, the trier of fact may be informed of all payments from collateral sources which are available or have been made to the party. If evidence of a collateral source is introduced, then evidence of any setoff or subrogation; setoff or subsequent rights; or premium or other payments made by or on behalf of the party may be introduced."

Sec. 2. This act shall become effective October 1, 1987 and shall apply to all actions filed on or after that date.

A BILL TO BE ENTITLED
AN ACT TO CHANGE THE STANDARD OF PROOF FOR THE AWARD OF PUNITIVE
DAMAGES AND TO ELIMINATE PUNITIVE DAMAGES BASED ON VICARIOUS
LIABILITY.

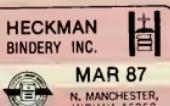
The General Assembly of North Carolina enacts:

Section 1. Chapter 1 of the General Statutes is amended by adding a new Article to read:

"Article 43E
"Punitive Damages.

"<1-539.25. Punitive Damages.--Punitive damages may be awarded to a plaintiff in a civil action only upon a showing of damages which are the result of intentional or of willful or wanton acts on the part of a defendant and only when those damages and the nature of the acts are proved by clear and convincing evidence. No punitive damages may be awarded to a plaintiff based solely on the vicarious liability of a defendant."

Sec. 2. This act shall become effective October 1, 1987 and shall apply to actions filed on or after that date.



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